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THE TOTALITARIAN STATE AND THE CLAIMS OF THE CHURCH

BY PAUL TILLICH

I. THE IDEA OF A TOTALITARIAN STATE

I

IN EVERY historical event there are certain inherent structural forces which are characteristic of a definite condition of society. Every historical event also involves accidents, natural occurrences, the activities of particular individuals and the influence of external historical happenings. In so far as an event is determined by inherent structural necessities it is capable of being traced and interpreted. In so far as it is dependent on chance it can only be established and described. The attempt will be made in the following presentation to deduce the idea of the totalitarian state and its practical application, particularly in Germany, from the structural necessities of contemporary social conditions and to interpret them in their wider historical relationships. This does not mean, however, that the occurrence of these events and the manner in which they took place were altogether independent of a surprising succession of chance events. I do maintain, however, and I think I shall demonstrate it, that certain inherent structural forces have found theoretical expression in the idea of the totalitarian state and practical realization in the attempts to bring such a state into being.

Structural laws and their resulting historical necessities seem the more general and vague the more the framework in which they appear is extended. And the scope allowed for concrete realization is greater. On the other hand they are more individual and definite and of narrower scope when the framework is smaller. Consideration from both wider and more restricted viewpoints is necessary when dealing with historical knowledge, particularly when con-

cerned with a contemporary idea which lays claim to universal applicability. From a wider point of view such an idea appears to possess fundamental significance as well as the character of necessity and historical world significance. At closer range, however, its fundamental significance becomes diminished and it takes on the character of a transitory and chance phenomenon. For the contemporary observer there is no certain assurance as to what perspective, what appraisal of significance or what admixture of necessity and chance are appropriate. He is obliged to paint into his historical picture as much of the coloring of "necessity" as he possibly can. Enough of chance still remains. Such a procedure is made necessary not only by the manner in which the idea of the totalitarian state arose but also by its conflict with the church and the claims of the church. This conflict is so fundamental and touches upon such old basic problems of Christian life that it calls for a consideration of the problem in its widest aspects. The church is being opposed by tendencies such as have not arisen since the conflict with the Roman Empire. Even if the struggle is to be fought out on German territory alone it is still of such general and fundamental significance for self-conscious Christianity that it can be solved only from the standpoint of a general explanation of the condition of present day society.

Although it is impossible to limit precisely the scope of the question, it is nevertheless inevitable in an article such as this that the author will have to restrict himself to mere indications of many questions. Some of the material which is only briefly touched upon here is developed at greater length elsewhere. I refer the reader especially to my book, *The Religious Situation of the Present*, and to my article, "The Religious Situation in Germany Today," published in *Religion and Life*.

There are three groups of tendencies from which arose the idea of the totalitarian state and the attempts to bring it into being. The first and most comprehensive group is concerned with the world situation of late capitalism. The second and intermediate group has reference to the postwar situation in Eastern and Central

Europe and the third and most limited group applies only to the German situation.

2

The world situation of late capitalism presents the following picture: the interconnection between all parts of the earth, which has been brought about by capitalist expansion, has resulted in a general and mutual interdependence in both economic and political spheres. It is the era of world wars and world crises. The political and economic system of the world is so interrelated that any injury to one part is bound to exert a detrimental effect upon the whole structure. Efforts for economic security and peace, therefore, are the common concern of all interrelated nations. At the same time and in a peculiarly contrasting way, however, all attempts at effecting such security upon the foundations of late capitalism are doomed to failure. For the physiognomy of the world reveals a second aspect: the constantly diminishing latitude for the development of capitalist dynamics forces every national group to intensify its own political and economic aspirations and thus aggravate political conflicts and economic crises. The present world system is fundamentally fluid and cannot achieve any stability on the basis of its own peculiar structure. The menace to our historical existence has loomed up tremendously in the epoch of late capitalism.

There are two ways of meeting this menace: either a radical amalgamation or a radical separation of the interconnected parts. The first attempt, which has long been tried in vain and which has not as yet been entirely given up, was directed toward political and economic amalgamation. This attempt may be considered as having failed. Hand in hand with this failure came the opposing tendency, which has led to growing economic isolation and to the aggressiveness of one political group against another. With this development the evaluation of the nation as a closed and economically self-sufficient political entity has made enormous progress. The belief in the armed and powerful nation as the last

stronghold of historical existence seems to be the result of the failure of the forces of amalgamation.

The effects of the world situation with respect to the special social groups are similar. The general insecurity of proletarian existence becomes aggravated by long periods of unemployment. And a new social group emerges, in which the negative aspects of the proletarian fate become multiplied. The exclusion from employment removes the last vestige of the meaning which work, even in the service of profits, can give. Of even greater importance is the threat of decline in social prestige and of economic proletarianization through overproduction and crises which confronts the commercial middle class, the groups of lower officials, clerks and peasants. Lastly even the ruling capitalist group exhibits an inner sense of insecurity which expresses itself in a feeling of bad conscience and in tendencies toward the suppression of competition and toward the utilization of state aid. The proletarian movements, when the threat to historical existence was first experienced, made the attempt to meet this threat by the elimination of class rule and by a supernational organization of political and economic groups. The newly threatened middle class groups have chosen the opposite course. They look to the national state for the security of their political existence, to measures of the national state for security of their economic existence, and to the winning over of the power of the national state for the purpose of establishing the security of their social privileges and class domination. They reject all supernational political or economic amalgamation such as was envisaged by the proletariat or even by the liberal bourgeoisie. The remnants of the feudal classes—the nobility, the hierarchy, the military and the upper bureaucracy—are, naturally, favorably disposed to this movement. The support of a large section of the new class of permanently unemployed may be explained in part by their opposition to those elements of the working classes which are relatively secure and partly by their own desperate position which drives them into the arms of any movement which promises immediate salvation. The same applies to the youth among these threat-

ened groups, who feel themselves robbed of their future. For all these classes the only security against the social threats and against the consequences of the world situation seems to lie in a strong national state, independent of the outside world and capable of independent action within the state.

This economic and political danger corresponds to a spiritual and psychical disintegration of the masses such as may only rarely be observed in history. The dissolving force of bourgeois society as regards inner security of either individual or social life, customs and morals, tradition and authority, faith and church has often been described. It has led to the mass disintegration of the proletariat; it has destroyed the effective forces of bourgeois society itself and now it has made wide inroads into the border groups of bourgeois capitalism, into the stagnating groups within the capitalist nations and also into the pre-capitalistic nations. Following the disintegration of the proletariat came an ever increasing disintegration of all groups as well as of all peoples linked with the capitalist system. This has resulted in making reintegration the central problem of late capitalism. Reintegration includes political and economic security as well as spiritual and social security, and also concerns the entire world which is enmeshed in one way or another in the late capitalistic scheme. The menace to historical existence, the growing disintegration and the yearning for security and new integration are everywhere apparent. In some instances it is the World War, in others the world crisis, which is most responsible for the latent feeling of insecurity and which has raised the question of possible security. In some cases disintegration has received its impetus from the religious secularism engendered by the propaganda of enlightenment among the masses and in others from the dissolution of forms of life through changes in social stratification. Often it is the product of all these factors. In all cases, however, the national state is looked to for a solution. The roots of the national state, it is true, are found in the anti-feudal bourgeois Enlightenment, but it has undergone a fundamental structural transformation in relation to general capitalistic developments. It

is at present much more in the service of all those tendencies which are in opposition to bourgeois democracy. Even where a communist world organization of economy and politics has been aimed at, the first and at present the only form of realization is the national state, as evidenced by the Russian example. Where a liberal world organization is attempted, as in the case of the League of Nations, final recourse is also more and more to the concentration of national political and economic forces. Such concentration, however, means that the national state must make itself as independent of the outside world as possible and internally must be prepared to act so that the program for security and reintegration may not be endangered by forces of disintegration. The fundamental liberal principles and constitutional rights, such as the separation of legislative, executive and judicial powers, the protection of private rights before the law and in social and economic life, the freedom of public criticism, political party struggles and economic class struggles, the wide latitude for conflicting ideologies, all these principles are considered as disintegrating forces which limit governmental freedom of action. The limitation of these rights and liberties may even appear inevitable in order to guarantee security and reintegration of the whole. Although the idea of a totalitarian state is not yet implied by these conditions they do present the first general and decisive prerequisite for its emergence. This is what will here be called "concentration of the national state."

3

The idea of a totalitarian state could never have arisen without the more limited anti-democratic tendencies appearing in Eastern and Central Europe. The peculiar position of these countries during the postwar period introduced a new element into the conception of the state. This was the idea that concentration of the national state is possible only in an anti-democratic and authoritarian form. Even in countries with older democratic foundations there was an increase in the authority of the state in relation to national concentration. Special powers were delegated to the government,

national truces served to restrict internal political battles, the constitution was adapted to the needs of the current situation and other measures of the kind were adopted. Fundamentally, however, the democratic basis in these countries has thus far been questioned only by small and relatively uninfluential groups. In Eastern and Central Europe the case was different. Here the anti-democratic attitude became elevated to a theoretical principle. At the same time the idea of national concentration assumed a more militant character. Inner concentration was, no doubt, hastened thereby but at the same time (in the dialectic used above) it increased the insecurity of the world situation and thus brought the desire for national security and reintegration to an inner contradiction, the consequences of which may be seen in the increasing danger of war.

The militant nationalism of Eastern and Central Europe is based upon three factors. The first is the establishment between the Baltic and Adriatic Seas of new national states whose first historical task is the consolidation of their national security. The second factor is the will of the nations defeated in the World War to regain their position of political power, wholly regardless of whether this power is to be used for war or not. The third factor is the dissatisfaction of certain of the victorious nations with their success, which was far below the national aspirations aroused during the war. The influence of this ever increasing militant nationalism upon the conception of the state is very apparent. Only authoritarian concentration of all forces and the ejection of all resisting tendencies provide a guaranty for the effectiveness of a militant nationalism. Only such a militant nationalism can secure the thorough and potentially military organization of an entire nation.

Militant nationalism receives support from the anti-democratic content of the culture of Eastern and Central Europe. Peoples like those of Russia and its border states never experienced democracy. They either maintained the feudal absolutist tradition or immediately established Bolshevik rule. In Central Europe the bourgeoisie, which remained in political and military dependence upon the feudal classes, was very ready to sacrifice democracy and sub-

ordinate itself to a new and purely authoritarian form of government, in order to ward off the threat of socialism. When the danger of a proletarian dictatorship after the Russian model seemed to be imminent an alliance was quickly effected between the remnants of the old feudal ruling classes and the traditionally subservient middle class. Militant bands, consisting of the unemployed and the youth, were formed and in this way the state of national concentration was turned into a militantly nationalistic and authoritarian state. It is obvious that the fundamental liberal rights and constitutional principles, above all the right of public criticism, were not only temporarily restricted but were either entirely or partially abolished. Of course all this is more characteristic of the general tendencies than of their actual realization. There are exceptions such as Czechoslovakia and there are weaker countertendencies to the authoritarian principle, such as the structure of the Communist party in Russia or the limitations upon the autocratic tendencies imposed by the bourgeoisie and peasants in the succession states. In these regions above all, the third element, the totalitarian state, is absent in theory, practice or both. In Germany alone are found both the theory and practice of the totalitarian state.

4

The widespread tendency toward national concentration of the state emerged from the insecurity and disintegration of the world situation during the period of late capitalism. In Eastern and Central Europe it assumed the character of a militant national and authoritarian state. It reached its fruition in Germany with the theoretical and practical realization of the idea of the totalitarian state. There have been instances of state intervention, particularly in the spheres of economic and social life, even in the older democratic countries. They were, however, neither fundamental nor totalitarian in character. The totalitarian tendency is very much stronger in the militantly nationalist and authoritarian state. Fascism has taken over not only those spheres, such as radio, press and film, which it deems necessary for the security of its authority;

it has also imposed a censorship upon certain aspects of scientific learning, it has set up definite restrictions in education and it has subjected, ideologically at least if not practically, all economic life to its authority. Even leisure time, to a certain extent, has been appropriated. But neither in Austria nor in Italy has there ever been a claim to a totalitarian state. In Russia the totalitarian state has been more effectively realized than even in Germany. Economic life, culture and education are all equally subject to state centralization. The motivating force behind this subordination, however, is not the state but the individual and the full development of his collectivistic activities. This is due to the special situation in Russia, which has set for itself the task of assimilating the rational technological culture of the past centuries of European civilization, and making it the foundation of economic life, education and culture, without accepting Western capitalism. The totalitarian character of the Soviet state, therefore, is to be understood on the one hand as a bulwark against the penetration of bourgeois-capitalist elements and, on the other hand, as the education of an entire continent in communistic enlightenment. Every step forward in this educational process means essentially a strengthening of the critical, anti-authoritarian and anti-totalitarian forces among the people. Thus the more successful it is in the realization of its goal the closer does the totalitarian state come to digging its own grave. This corresponds precisely to the theories of Marx and Lenin on the state. According to them the state as a form of political power is ultimately to be dissolved into a free and self-administering society.

The totalitarian dogma as developed in Germany represents a complete contrast. Although it has not been carried out in practice as radically as in Russia it has taken on a much more fundamental significance. Only here has the idea been systematized as a theory, because the disintegration of late capitalism has advanced farthest in Germany and therefore has aroused more intense passions, and because of the traditional Prussian-German political thought, which received its strongest expression in the formulations of the older and earlier organological school but which was also echoed in the

writings of Hegel. Out of the interaction of both factors has come the dogma of the totalitarian state.

The assertion that disintegration has advanced farthest in Germany does not apply to the almost heroic attempts of various individuals and parties during the republic to battle for security and reintegration even at the risk of personal and political self-sacrifice. It refers much more to the fact that Germany manifested more acutely all the factors in the threat to traditional society as revealed in the world system of late capitalism in general and in Central Europe in particular. The reasons are quite evident. One of the most important, particularly from a psychological point of view, was the Treaty of Versailles. In addition there were the internal political, economic, social and cultural factors which are rooted in the particular structure of Germany. These have been reenforced by the peculiar destiny of the German people, a destiny which reveals both greatness and tragedy. For Germany has experienced the age-old contradictions of Western history in a fundamentally more acute form and at the expense of its own unity. Only in the light of these facts can one understand Prussian political mysticism. Ever since the Reformation and the Peasant War, above all since the close of the Thirty Years' War, the unified religious, social and cultural foundations, which in other nations made possible extensive limitations of state influence, were completely lacking in Germany. Only the state seemed able to assure the security and integration of all vital forces in the nation. Thus the organological school raised the state to an independent reality above all individuals and Hegel included the entire social and moral life within its scope. In Hegel's own system the power of the state was regulated by strong corrective forces which sprang from his bourgeois conceptions of freedom. After the discarding of these correctives and the complete triumph of the organological concept the way was prepared for the elaboration of the idea of the totalitarian state. A hundred years after Hegel's death this step was made possible by the new political and social conditions.

In view of the fact that the world crisis is to be understood pri-

marily as an outcome of the world economic situation of late capitalism, the totalitarian state found it necessary above all to become master of the economic sphere. Such was the case in Russia even without the totalitarian theory. Although the subordination of economic life to the state was given clear theoretical enunciation, its realization met with the resistance of the capitalistic leaders and of the tendency of general economic development toward the emergence of a semi-feudal and monopolistic ruling class. A very patent gap in the totalitarian system thus remained, which has been covered up to some extent by emergency economic measures of the state. It is impossible at this time to predict what the permanent effects of this gap will be upon the totalitarian state: whether it will become wider, and disrupt the entire system, or narrower, and strengthen it. The claims of the totalitarian state upon the cultural spheres, education, science, art and social life were correspondingly greater. A presupposition for this was the suppression of all the fundamental rights of the individual, the concentration of all powers in the hands of a person responsible to no one and supreme even in matters of law, and the rejection of all constitutional correctives. Thus was provided the most extreme reenforcement to the totalitarian factor. Even the leadership principle, in its original sense, was subordinate to this tendency. In charismatic leadership there is something unique and non-institutional; there is a sort of dependence upon the free inner as well as the external recognition of those who are led. But as soon as the leader transfers his personal authority to the authority of his office the interrelationship between the leader and his following is lost even if there is an attempt to maintain it. The original restricted power of personal authority becomes transformed into a derived but unlimited power of the authority of office.

5

The concentration of all spheres of life within the unlimited authority of the national state is possible only when founded upon a world view which has the inherent power of encompassing man's

entire being and driving him on to unconditional self-surrender. Such a world view is religious in character and finds expression in a myth.¹ The more unconditional and more inclusive the claims of the state are, the more fundamental and powerful must be the myth, which is the foundation of such claims. In an older democratic society national concentration requires little of this mythical element in order to make itself effective. As in the case of the United States, any threat to its historical existence is sufficient to bring about the use of rational measures to effect security and reintegration. The question as to the permanence of the effects of such measures belongs to the future and upon its answer depends the destiny of these nations. The authoritarian state, however, requires a more powerful foundation, especially when it deprives the individual of his fundamental rights. In many instances, as in Austria and other succession states, the development of a militant nationalism is sufficient to reenforce the authority of the old secular and ecclesiastical hierarchies without the need of a new myth. When the totalitarian tendencies are more powerful new myths are required in order to provide the basis for the struggle and for reconstruction. In Italy, for example, there is the myth of the Roman Empire, which is used for this totalitarian purpose. In accordance with the purely political character of this myth, however, it leaves the religious life entirely free and, as for education, it is able to come to an understanding with the church. In Russia the more powerful totalitarian tendency is bound up with the influences of deeper mythical forces. Marxist dogma, it is true, is considered a science. The mythical quality of the dogma, however, cannot be disputed. It is invested with the force of dogma and is not permitted to be questioned and, with its eschatological enthusiasm and expectation of a world of justice, it has released the tremendous energies which brought about the revolution and the defense and

¹ The ideas of myth and mythology are used here, as in other instances, not in the sense of creations of the imagination but rather in the sense of real but conditional forces which have been elevated to the rank of absolute sanctity. The myth, therefore, possesses reality, but it also transcends reality in passing over into enthusiasm and mysticism.

reconstruction of the Soviet state. The totalitarian claims of the Russian state rest upon the myth of social justice, which, in the form of a rational doctrine, provides a foundation for the entire life of the Russian people.

The basic conceptions of the totalitarian state, as revealed in the German situation, are tied up with the strongest and most conscious elaboration of the myth. A series of intimately related mythical ideas have come to exercise a great influence and a national mythology has developed centering around the myth of "the nation" (*Volk*). Revolving around this idea are other myths such as those of blood, territory, race, state, leadership, etc.

The mystical character of the myth of the nation is clearly to be seen in the work of the leading theologian of the German-Christian movement, Emmanuel Hirsch (*Die gegenwartige geistige Lage*, Göttingen 1934). Hirsch speaks of the nation in essence (*Volkstum*) as the "mysterious sovereign" (*verborgener Souverain*) whose ends all state activity must serve. The nation is to be founded upon the "mystery of the blood covenant" and the state authority upon the blood relationship of leaders and followers. The individual member of the nation has no real existence outside of this union of blood. His historical existence is based entirely upon his membership in the national group and his actions must follow the will of the "mysterious sovereign," which becomes manifest through the leader. His goal must be the realization of whatever is best for the creative and determining forces in the nation. The triumph of this myth and the reality from which it proceeds over all opposing forces represent the "sacred hour" of the nation, which must be experienced with enthusiasm and unconditional surrender. It is the "fullness of time," in the religious sense of the term. "Even the harshest measures of the state," even the resolution of the entire life within the state, is necessary and sacred if it serves the purposes of the nation, the "mysterious sovereign." He is not God, but he is an immediate revelation of God.

This is the totalitarian state, born out of insecurity of historical existence during the epoch of late capitalism and designed, through

national concentration, to create security and reintegration. It arises in Central Europe where liberal rights and democratic tendencies have been displaced by a militant nationalism and an old feudal authoritarianism. In Germany, where disintegration and insecurity have become most palpable, it receives theoretical elaboration, is nourished and suffused with the powers of myth and carried into effect with passion and unscrupulous consistency. It has received mystic consecration and stands, not merely as the earthly representative of God, as Hegel conceived it, but actually as God on earth. A God or a Demon! Whether it is a god or a demon is determined by its relation to the Christian church. Does and can the totalitarian state stop short of the church? Must it not clash with the claims of the church and become involved in a life and death struggle with the church, irrespective of whether its leaders desire it or not?

II. THE CLAIMS OF THE CHURCH AND ITS CONFLICT WITH THE TOTALITARIAN STATE

I

The claim of the church is based upon the absolute character of its teaching. Its gospel consists of proclaiming God in the sense of the first commandment: "I am the Lord thy God, thou shalt have no other gods before me." Every word of the Old and New Testaments is a further development of these words. The whole Bible is concerned with the divinity of God as opposed to any human claims. This is revealed in the words to Abraham: "Get thee out of thy country and from thy kindred and from thy father's house unto the land that I will show thee"; in the prophetic tirades against the pagan national gods and the religious nationalism of the false prophets of Judah; in the proclaiming of the Kingdom of God, embracing all peoples and destroying all the national world empires; in the crucifixion of Christ and its interpretation by the Apostle Paul as a judgment passed upon every human force and agency, every nation and religion which arrogates unto itself the

power of God; in the words of Jesus: "Thou shalt love the Lord thy God with all thy heart and with all thy soul and with all thy mind and with all thy strength," and proceeding from this, "Thou shalt love thy neighbor as thyself." In this respect there is no difference between the Old and the New Testaments. In the Old Testament the claims of God wage a battle for a people and with a people until this people is destroyed. The Old Testament, therefore, is not a national Jewish book but a record of the struggle of God against the national aspirations of Judaism; a struggle not in behalf of another national claim but rather for the triumph of God over any and every national pretension. The New Testament takes for granted the experiences of Jewish history and the idea that a nation cannot belong to God as a nation. The community of Christ, which is the true Israel, is therefore not a group of superior people of a superior race, but an assembly of all nations and religions. They are called by divine will, "through Grace alone," and therefore never sure of not being cast aside as a visible church as were the chosen people. This principle is strikingly revealed in all periods of church history. It appears with the Church Fathers who waged successfully the first battle for the Old Testament and thus prevented the dissolution of Christianity into a Pagan-Gnostic movement such as that desired by present day German pagans. Athanasius battled against the Arian interpretation of Jesus as a heroic demigod, an idea very familiar in the sermons of the German Christians. In Augustine it appears in his struggle against the belief that humanity has remained essentially untainted and in his forceful conception of the historical battle of the Kingdom of God against the Satanic kingdoms of the earth. Luther showed the same principle in his assertion of the sovereign rights of God to dispense grace, independently of any religious, spiritual or vital powers. Calvin showed it in his passion for the glory of God before which all human glories pale into insignificance and in his subjection of all peoples to the unity of the Kingdom of God which is to descend upon earth. This point has never been seriously questioned in principle in Christianity. Therefore in Germany

Christians of all confessions have joined in a common opposition when this cardinal principle of their gospel, the supremacy of God, has been laid open to question by placing other gods beside Him.

2

The claim of the church is based on the claim of God as proclaimed by the church. It is not identical with it, however, for the Kingdom of God and the church are not one. The church proclaims the coming of the Kingdom of God but it comes not only in the church. The church points the way to the Kingdom of God but the church may also serve to hide it. Various possibilities proceed from this dialectic relationship which emphasize the proximity or distance of the one to the other. The most dogmatic assertion of the identity of the Kingdom of God with the church is found in the Roman Catholic church; the separation of the two is expressed most clearly in genuine Lutheranism. Various gradations exist between these two positions. Of these we will here concern ourselves with the Greek Orthodox church and with Calvinism. A decisive factor in the relation of church and state consists in how far a church lays claim not only to the inner life of man but also to his external and social life, and how far it thus assumes a character similar to that of a state.

Roman Catholicism, with its political organization and its hierarchic structure, goes farthest beyond the immediate religious life. Grounded in Thomistic social ethics and aided by the political power of its followers in various states, it aspires to spiritual leadership in all aspects of life relevant to religion—therefore in all spiritual, social and communal life and its legal and political forms. It leaves in the hands of the state the immediate exercise of power for the ordering of life but it cannot concede to the state the determination of the content of human life. For the content of life is unconditionally subject to the claims of God and the church is responsible for its realization. The church, therefore, makes unconditional claims upon education and considers it a question which involves the very existence of the church. Despite its formal

recognition of the supremacy of the state in education, it inevitably penetrates the content of this education.

In the case of the Greek Catholic church, particularly in Russia, the situation differs in the respect that there never was a political hierarchy. In contrast to Protestantism, too, there was no active communal life. A religious and political title to leadership or a direct influence upon the religiously relevant spheres of life could not, therefore, come about. The Russian church was united with the state in the person of the Czar, and when this point of union was destroyed the church as an organism collapsed. The Russian Christians, however, lay claim to the sacred traditional cult and to the power to exercise and order this system of rites. On this point no compromise with the scientific dogmas of Bolshevism is possible.

Calvinism lays no claim to the absolutism of the church as such, but rather to the Will of God, proclaimed by the church and found in the Scriptures. This pertains not only to the inner life of the individual but also to the life of society. Thus Calvinism has set up norms not only for the doctrines of the church but also for its organization. Hence the struggle for the divinely ordained church organization and for the public influence of the church. Hence also the feeling that the Kingdom of God is progressively realized by the Christianization of society through the preaching and teaching of the church.

Early Lutheranism espoused no definite and divinely ordained constitution or social order. Any constitution was tolerated which permitted the unrestricted propagation of the pure doctrine through word and sacrament. Lutheranism thus can subordinate itself to any social order or political structure without attempting to exercise any direct critical influence. Only indirectly, by virtue of the fact that office holders are Christians, does Lutheranism attempt to infuse Christian spirit into those secular phases of life which are of religious consequence (*cf.* the social legislation of Bismarck). It is only through this separation of political from private morality, a fact which is historically understandable but

in its ultimate effects quite disastrous, that one can explain that absence of public criticism of state activities which seems so incomprehensible to Anglo-Saxon Calvinism. It is this too which explains the silence of the Lutheran church on the boycott against the Jews, but which also explains the passionate struggle against the application of the Aryan clause within the church. The severely anti-clerical and anti-religious currents in the revolutionary labor movement in Germany are also explained by the absence of public political criticism on the part of the Lutheran church. The failure of the religious socialist movement, which attempted to widen the horizon of Lutheranism by going back to genuine Christian and particularly Augustinian traditions, is also largely attributable to this Lutheran separation between private and political morality. It is not altogether unfair when early Lutheranism is charged with adopting Machiavellian social ethics.

The conclusion derived from these considerations may be briefly summarized as follows: all churches must claim the right to preach without hindrance and to realize within the church the divinity of God and his unconditioned supremacy in the world. The Catholic church deduces from this the demand that the hierarchically constituted church should direct the entire religiously relevant life of the people. The ultimate consequence of this demand is the mediaeval belief—and it has never yet been given up—that every political hierarchy must subordinate itself to the spiritual and priestly authority. The Greek church demands freedom for the preservation, exercise and interpretation of the traditional system of cults, with complete indifference to political and social problems. Calvinism demands the right to a freely elected church organization and the possibility of free exercise of influence by the church upon public life and the political decisions through which public life is formed. Lutheranism lays claim only to the unrestricted propagation of the pure doctrine and is inclined to leave all constitutional and administrative matters to the state.

All churches thus lay claim to one thing in common: to place man before the presence of God—whether it be through priestly

mediation, through cult and sacrament, through proclaiming God's will in the world, or through the preaching of true doctrine. For this goal they lay claim to man's deepest experience and to all aspects of his existence. So long as they are what they are, churches, they cannot give up this claim.

3

The Christian churches have no inherent reason for resisting national concentration in itself. Although from the standpoint of the expectation of the Kingdom of God they must welcome all tendencies toward uniting the forces of humanity, they still cannot overlook the danger to the historical position of the nations and the break up of the forces that united them. They must, therefore, affirm and support every attempt at historical security and reintegration, therefore also the concentration of the national state in so far as it serves this purpose. But their task to keep alive the feeling of both an original and a future unity of mankind still remains.

One should not expect any resistance on the part of the churches to the anti-democratic and anti-liberal position of the militantly nationalistic and authoritarian state. The ecclesiastical hierarchies are at all times ready to renew their old alliance with the political hierarchies if it means the strengthening of the authority of both and an extension of church influence. This is revealed most patently in the alliance of the spiritual and the secular reactionary forces in Austria. The churches do, indeed, surrender many and often very decisive aspects of the claims which they are in duty bound to assert, above all in reference to social justice and the unity of mankind. This is a part of their general culpability, which has always caused the emergence of passionate opposition based on the very principles of the church. These ever recurring phenomena show the willingness of the churches to accept compromises with the ruling state power whenever it is agreeable to them.

The circumstances under which they reject compromise must therefore be very much more serious. Such circumstances arise when the state intervenes in the church itself or else in those

spheres which the church is convinced will have to remain subject to the church. The actual occurrence of such intervention or the belief by the church that such intervention is taking place naturally depends upon the general complex of historical events. In Italy, despite strong totalitarian tendencies, the state was able to establish an accord with the church by not making any claims upon factors of ultimate and external importance.

In Russia, on the other hand, there were serious conflicts. Marxist dogma, which is the foundation of contemporary Russian society, contains two elements. One is what we have termed the myth of social justice. With the substance of this myth the church has no controversy. On the contrary, it would be in duty bound to fuse this substance with its own doctrines after having removed the mythical-utopian elements of it. The church could and would have to give meaning to this substance and refashion it from the standpoint of the expectation of the Kingdom of God. A conflict on this question is possible only where the church, in contradiction to its mission, has become so intimately allied with definite social groups that it supports their struggle against the demand for social justice, or else when it feels bound to raise objections to the demonic methods of the revolutionary struggle. Neither of these conditions has led to the present day conflict. It is rather the second element of Marxist dogma which is responsible for this conflict. This is the anti-religious form in which, for certain historical reasons, Marxism developed in Germany and was taken over in Russia. The claim of the state to fashion the entire life of man in this spirit inevitably clashed with the mystical and ritualistic tradition of the Russian Orthodox church and, despite the complete political passivity of the church, led to the attempt to eliminate it from any position of influence. It is true that the struggle has been carried on chiefly by the independent Godless movement rather than by the state itself. The state measures, however, have resulted in such a far reaching debilitation of the church that in many ways it has already been proclaimed dead. It is not dead, however. Its inner existence is threatened, but less by terroristic acts than by the

atheistic education imparted to the youth. The struggle against the Russian church is to a great extent a struggle against the Russian Middle Ages. This accounts for the weakness of the Russian church, which is in a position similar to that of the Roman Catholic church during the French Revolution. But just as the Catholic church was ultimately able to assert itself against bourgeois atheism, so it may be expected that the Russian church will also assert itself against the proletarian atheism. The claims of the totalitarian state upon those parts of the human soul that are outside the technical and political realm will have to be surrendered here as in the former instance. And the churches in their turn will be forced to surrender their mediaeval claims. This problem, already settled in Western Europe, is the basis of the conflict between state and church in Russia.

4

The situation is quite different in Germany. Here there is no mediaevalism to conquer. There may be rather, as one often hears said, the dawn of a new middle ages. Problems are emerging which have not arisen since the beginning of the Christian Middle Ages. Since the triumph over ancient paganism and the Christianization of the Germanic tribes there has never been any independent non-Christian myth which gave the state unconditioned sway and which was made the foundation for the totality of life. This has now occurred in Germany, and with it has come a host of problems. The totalitarian claim of the state upon man clashed with the unconditional claim which God makes upon him. The myth of the German nation and empire confronted the message of the people and Kingdom of God; the myth of blood, the community of sacrament which transcends blood relationship; the unconditional tie of the individual to his nationality, the requirement to be able to leave homeland and father's house for the sake of God; the disparagement of the individual, the doctrine of the absolute value of the human soul; the leadership of the national state, the sovereign claims of Christ; the coordination of the spirit,

the directing judgment of the Spirit of God; the consecration of the present, the hope of the future. The destiny of both the totalitarian state and the German churches, with either their possible union or their fundamental irreconcilability, is involved in the conflict between these opposing currents.

Every created reality has its value as creation, but its worth is derived not from itself but from the creative foundation from which it springs. It is finite and transitory but it becomes blasphemous when it aspires to be infinite and unconditioned like God. Everything finite is guilty of such aspiration. This is true not only for the individual but also for all powers and creations of nature and history. It is also true of races, peoples, states, leaders and their followers. They can be elevated to the state of unconditioned worth only by wanton contradiction of their finite character. They attain to this state, however, as soon as they are spoken of, experienced and acted for, as if they were gods. The way in which this myth of the nation is propagated and the resulting activities are indications of such a tendency to attribute an absolute character to a conditioned being. If the expression "Myth of the Twentieth Century" is to be taken as seriously as it wants to be taken then it elevates the nation to divine dignity and the believers in this myth cannot but draw the practical consequences from it. The simultaneous recognition of Christianity may mean only that the Christian tradition as a whole is too deeply rooted in national consciousness to be eradicated; but it must subordinate itself to the criticism of the new myth, that is, it must either be set aside, transformed or changed.

This has been attempted in various ways, such as the subordination of education to the propagation of the new myth, the rise of a frankly pagan religious movement which aspires to recognition as an independent church, or, above all, the attempt of the new mythical tendencies to penetrate into the old church organizations. Such manifestations reveal the earnestness and zeal with which the consciousness of the new myth determines the thought and acts of its adherents. The individual points of conflict between the new

myth and Christianity are unimportant so far as concerns the general mythical position. Nevertheless they are symptoms of great interest. There is above all the attack upon the Jewish prophetic ideal of piety and upon the use of the Old Testament as a book of religious instruction for the German people. There is also the supremacy in the national church of blood relationship over community of sacrament. Or there is the attempt to displace the highest Christian values of humility, love and hope by the supreme pagan virtues of courage, power and enthusiasm, and thus to transform the New Testament image of Christ into that of a heroic figure. There is further the division of truth and justice into as many truths and ideas of justice as there are national spirits and corresponding national states. This accounts for the rejection of the prophetic transcendental criticism of state measures in so far as they serve the ends of one's own nation—for the nation is the "mysterious sovereign" and the final norm. There is no doubt that this idea stands in sharp contrast to the ideas of the New Testament, according to which all "mysterious sovereigns," angels and powers, have been vanquished and brought together in the cross of Christ. The new myth contradicts the unconditioned character of unconditioned beings and thus the mission of the church and the claims which it cannot surrender. This myth, however, is the basis of the totalitarian claim of the state.

5

The idea of totality contains a mythical factor within itself. Only that which is absolute can lay claim to totality. Were it not unconditioned it would have something else whereby it is conditioned; it would have to concede a sphere alongside of its own sphere and would thus have to circumscribe its totalitarian claims. Since a mere juxtaposition of spheres destroys the unity of man and the world, there is the quest for a third and higher entity to which both spheres are subordinated. The conflict between the totalitarian state and the church can only be understood in the light of this dialectic of conditioned and unconditioned.

The state attempts to avert the conflict in two ways: first, directly, by separating the spheres, and second, by inner assimilation of the spheres of the church. The first way is the official state method, the second is the ecclesiastical political method. The first method is formally applied to all churches, the second only to the evangelical state churches. The state has always declared that the churches, i.e. dogma and ritual, were to remain free from state intervention, that public education was to be based on positive Christianity and that all atheistic propaganda was to be forbidden. The concessions in the concordat with Rome go much farther in some points, such as in the education of priests, than any other government has gone. The magnitude of the movement back to the churches seems to show that there is a strong, even though unofficial, political pressure behind it. The church organizations, in so far as they serve ritualistic purposes, are not suppressed. The Aryan paragraph has not been enforced in specific Catholic schools and hospitals. There seems to be a wide latitude of independent activity which the state has allowed to the churches, particularly to the Catholic church. The state thus seems to have effectually limited its totalitarian claims. It is also no doubt true that the churches would be ready to utilize for their own purposes the strengthening of their influence upon the people, the elimination of anti-clerical propaganda and the anti-liberal authoritarianism had not the fundamental opposition to the new myth deprived of their value all the elements of community.

It is impossible to isolate the dogmatic and ritualistic spheres and place them beyond the sphere of real life. There are aspects of life which are further removed from religious claims than others. Man's technical activities in all fields, including the political, have no direct relation to religion. They are subject only to the laws of utility. But every use points to a higher use for which it is but a means, and they all point to an ultimate goal which is an unconditioned and determining principle. From this standpoint the transcendent claim, religiously speaking, infuses divine necessity into all worldly spheres. For this reason all advances made by the

state to the church are of no avail if these spheres, the most remote as well as the nearest, are subordinated to another determining principle; if, with its separation of spheres, it keeps the church and its claims far from the realities of life.

The sphere in which, up to a certain degree, all other spheres come together is that of the education of the youth, both in and out of school. It means but little to the church that it is accorded a far reaching influence on education if on the other hand the education by the state, and that means education based on the new myth, not only is imparted to the entire youth, but, with unlimited effectiveness, is made the necessary condition for all success in the life of the state. Those brought up in the spirit of church education thus become stigmatized as second rank citizens according to the new ideal image of a German man. It is evident that all other compromises become illusory in this light and that a struggle must break forth in which there cannot be any real compromise for the church.

There are inevitable sources of conflict from another side. The system of the totalitarian state and that of the Catholic church are both systems of unconditioned authority. It is, however, impossible for two unconditioned authorities to exist together without both becoming conditioned. For that reason each one must attempt to undermine the other. Symbolic of the situation is the fact that the fundamental book of the new myth has been placed on the Papal Index and that the sale of a defense of the Old Testament by a bishop has been suppressed by the party. This indicates that in the spiritual realm too a separation of spheres is impossible of realization as soon as there is a question of basic world views. A further symptom is the fact that the filling of all important posts of cultural instruction is now dependent not only upon the scientific institutions themselves but also upon a cultural commission of the party, which is under the influence of the propagator of the new myths. This is also a public confession of the impossibility of separating the spheres of interest.

Since it is impossible to deprive the churches of their own world

view and since no man can subscribe to two genuine world views, both of which provide the whole of the world and life with a meaningful principle, the individual finds himself forced to make a decision.

In the spheres of practical life this opposition has down to the present been of little consequence. This was due mainly to the fact that the conservative forces in the church were in accord with such anti-liberal measures of the state as involved the fundamental rights of the citizen. Also in Austria there were no conflicts on these matters. The limits of toleration of the church were reached when the right and the duty of the church to dispense divine grace through intercession and sacrament to those excluded by the state from its community and from life could not always be exercised. The restriction of this last human right in some cases has deepened the internal tension and sharply illuminated the contrast between the two world views.

6

The situation is quite different in the Protestant churches. Here there was also the possibility of indirect subordination of the church through inner ecclesiastical movements. The lay character of Protestantism, its democratic structure, the fundamental indifference of Lutheranism to questions of church constitution together with a profound and justifiable dissatisfaction with the rigidity and the aloofness of the official church circles, all made it possible to effect successfully a coordination of the church during the first period of the new regime. But the too rapid triumph was ominous. As soon as the new myth was made the regulating principle of church gospel in many places within the church and as soon as the attempt was made to transfer the race dogma and the authoritarian principle of leadership to the church, resistance arose. It became increasingly consolidated and has now taken on the form of a church within a church supported by world Protestantism.

It must always be emphasized in this connection that it is never

a question of political resistance to the state. Not only do the repeated professions of loyalty of the opposition leaders testify to this fact; it is also deducible from the essential character of Lutheranism. The Lutheran church, which has determined the character of Protestant Germany, has always left the extra-religious phases of life in the hands of the state, so that the church was confronted with the growing danger of disappearing from public consciousness. Every semblance of meddling in political affairs has always been avoided on the part of Protestantism in so far as it is a question of political matters only. The external constitution and the whole legal and administrative side of ecclesiastical life has, since the Reformation, been left by Lutheranism in the hands of the state, so that even now there would have been no difficulty in effecting an agreement concerning changes in the constitution and amalgamation of the state churches of Germany, had not the new myth brought on the break. The more evident this background of the ecclesiastical policy of the group of the Reichsbishop became, the deeper became the abyss between the two.

In this situation the oath demanded from every church minister appeared as a symbol. This oath meant, first, subjection to the church rule of the Reichsbishop. In the second place, the relationship between this subordination and the oath of loyalty to the state was made so close that rejection of the former would appear as disloyalty to the state. Third, the ecclesiastical oath was sustained by the state oath. This action of the Reichsbishop's synods has strengthened among many of the opposition clergy the determination for resistance even to martyrdom. This is very understandable in the light of church history. For that demand of an oath is reminiscent of the demand made upon the Christians of the early church to sacrifice to the emperor, in so far as it involves according recognition as a sacred power to the state. The early struggle was a tragic one: tragic because the existence of the Roman integration to the world seemed to hinge on the recognition of its sanctity. The almost unlimited toleration of the Roman state, which was far removed from totalitarian tendencies, became

limited the moment it and its emperor myth were exposed to contradiction. The almost boundless loyalty of the early Christians to the Roman state came to an end when another myth which demanded subordination came to vie with the gospel of one God and His revelation on the cross. It is undoubtedly true that the contemporary situation has not reached the acute stage of the early church period. The destruction of the pagan myth by centuries of martyrdom in the Christian church is an irrevocable fact which is also an obstacle to the pagan tendencies of today. But there are possibilities which can lead to an analogous situation. The contradiction of principles is present and it must have its effect even if there is the desire to avoid the struggle. It is inevitable as long as the state, on the basis of its determining myth, makes claim to an absolute and totalitarian character. Where the struggle is concerned with unconditioned and totalitarian principles, the separation of spheres is illusory. This is proved by the church struggle.

From the standpoint of the churches and their claim the conflict can be solved only if the new myth is overthrown and with it the totalitarian idea. National feeling and state, authority and leadership can be affirmed only within limits which recognize the unconditioned character of the absolute or, religiously expressed, the godly character of God, who tolerates no other gods beside Him. Within these limits the church can and should affirm them and desires to do so. What is beyond these limits the church must reject. It cannot put itself and its gospel at the disposal of the totalitarian state as its determining myth. There is no identity of political and ecclesiastical activity in Christian countries whereby the state may lay claim to the unconditioned character of church gospel and be able to make it effective by means of its own force, such as power, organization and technological methods. The contrast between divine and human reality must always express itself by distinguishing between a church which, although not absolute itself, gives evidence of the absolute and a state which has the task of regulating the finite and social sphere, and which therefore has no right to a claim of absolute or totalitarian character.

7

It is difficult to make any predictions regarding the outcome of the struggle. Perhaps the totalitarian system will be dissolved from within with the strengthening of the feudal capitalist tendencies and thus the churches will receive their necessary freedom of scope. Perhaps a church under the Reichsbishop will arise which will give free play to the new myth and which will be constructed on an authoritarian basis, more after the Catholic than the Protestant fashion, while the Protestant opposition will be organized into a free church. The danger of such a free church will be, as it is already, that, in order to defend itself successfully, it will have to clothe itself in the mail coat of dogmatic orthodoxy. Even in this narrow form orthodox Protestantism, like Catholicism which is socially pressed in another way, will break down the totalitarian system. The idea of the totalitarian state will founder upon the Christian church and gospel which will destroy the new myth.

These circumstances are of fundamental significance, since the events in Germany are to be understood only through the world situation of late capitalism. The internally concentrated and authoritarian national state, which always seeks to encompass new fields of life, lies within the compass of the general world situation. Development has progressed farthest in Germany where the totalitarian state was conceived and to a great extent realized. But in Germany too it has found its limitations. Security and reintegration at the price of a myth which destroys the force of the Christian gospel is no reintegration but the deepest disintegration—in the individual, in the nation and among the nations. For it replaces the God, who alone is God, by many conflicting gods. It rends the individual consciousness and it tears apart both the nation and humanity. The twentieth century will go to its destruction if the myth of the twentieth century triumphs. The struggle of the churches for their own claims is at the same time a struggle for genuine foundations of real historical reintegration.

MONETARY EXPANSION AND THE STRUCTURE OF PRODUCTION

BY HANS NEISSER

THE traditional writers on the business cycle have never doubted that a real monetary inflation is very likely to bring about eventually a severe crisis, however favorable its effects on employment might be in the beginning. But stabilization of prices was looked upon as the very opposite of inflation, though the term "inflation" itself remained controversial. It is Hayek's¹ merit to have raised doubts as to this oversimplified doctrine and to have examined first the question whether or not the increase of the money stream, necessary to stabilize the price level in an expanding economic system, must not produce the same dangerous effects as inflation in the traditional sense of the term. Hayek's results seem, however, to the present writer as one-sided as the viewpoint of the price stabilizers. His main proposition that in every instance an increase of the money stream cannot but bring about a real business cycle—boom, crisis and depression—is not sufficiently proved in the two central chapters of his *Prices and Production*. An active monetary policy seems by no means definitely excluded from rational consideration by Hayek's brilliant attack.

It is not the intention of the present article to examine the whole content of Hayek's little book and Mises' theory of the business cycle, more fully elaborated therein. We shall confine our analysis to an examination of the question whether or not every increase of the money stream, however restricted, must bring about temporary disturbances of the structure of production which could properly be regarded as phases of a business cycle; we shall then add some remarks on "sound" or "neutral" credit expansion.

¹ Hayek, F. A., *Prices and Production* (London 1931). I quote from the German edition, *Preise und Produktion* (Vienna 1931) only for passages that do not appear in the English version.

I

Forced Saving

If all the prices varied instantaneously and in the same degree when the volume of the money stream varies, and if all monetary contracts were adjusted at once to the varying price level, evidently neither the objection of the price stabilizers to a diminution of the money stream nor Hayek's objection to any increase in the stream (excepting only the doubtful case of a growing population) would be justified. It is to the existence of fixed debt contracts and to the rigidity of certain income rates, especially wage rates, that the significance of the absolute price level, in contrast to the system of price relations, is usually attributed. On these rigidities are based not only the apprehensions of price stabilizers as to the effects of a falling price level, but also the doctrine of forced saving imposed on consumers by a rising price level, or, according to Hayek, by an increase in the money stream. It suffices to quote in this respect Hayek himself, who describes the sacrifice imposed upon consumers by forced saving.¹ "This sacrifice . . . is made by consumers in general who, because of increased competition from the entrepreneurs who have received the additional money, are forced to forego part of what they used to consume. . . . There can be no doubt, that if their money receipts should rise again, they would *immediately* attempt to expand the consumption to the usual proportion. . . . But if it does [*sc.* if the consumers' receipts rise] then at once the money stream will be re-distributed between consumptive and productive uses. . . ." This process of "forced saving" runs as follows: some entrepreneurs, being provided with additional purchasing power by the banks, compete for certain capital goods and for workers in order to secure the desired expansion of their enterprises; in this way they establish a price of capital goods rising faster than wage rates and, eventually, a withdrawal of resources from consumers' goods industries which cannot pay the enhanced prices for them; the falling supply of con-

¹ *Ibid.* p. 52 ff. Italics mine.

sumers' goods causes a rise of prices also in this sphere, which, however, lags behind the price variation in the sphere of capital goods for a long period and therefore is not able to prevent the withdrawal of resources to the latter sphere. In this way, by forced saving, the same goal is reached as is usually reached by voluntary saving, namely a restriction of consumption and a devotion of a part of the productive resources to the production of additional capital goods.

We can accept this description of the mechanism of forced saving for the first part of our analysis, stressing, however, two points: first, that this description starts with the economic system in full equilibrium, and second, that nothing in the course of this process is altered if, as Hayek suggests in a more recent publication, we substitute for the assumption of the rigidity of contracts and certain income rates the assumption of a theoretically necessary lag between the increase of receipts and the increase of spending.¹ Forced saving would in this way be diminished to an almost negligible amount, but, so far as it still exists, it acts by diverting factors of production from the consumers' goods industry.

II

The Demand for Capital Goods: Business Fund and Savings Fund

The means by which forced saving is accomplished is defined above as an increase of the money stream rather than of the stock of money. The reason is quite obvious. It is generally agreed that

¹ Cf. Hayek, F. A., "Capital and Industrial Fluctuations" in *Econometrica*, vol. ii (April 1934) pp. 158-9. By the introduction of this new concept of forced saving Hayek is enabled to treat the rigidity of certain income rates and contracts as a merely "institutional" fact which may be disregarded in a discussion of general principles; thus is secured a way out from the obvious contradiction in *Prices and Production*, where Hayek assumes on the one hand perfect plasticity of all income rates and perfect adaptability of all contracts in the case of deflation, and on the other hand needs the mechanism of forced saving, usually based on the very rigidity of these rates. We doubt that forced saving, if not based on that rigidity, would have any practical importance. If income payments rose as fast as commodity prices the time lag between the increase of demand for capital goods and the increase of demand for consumers' goods would, on the average, amount to hardly more than one week, whereas the diverting of factors of production from the sphere of consumers' goods would certainly need more time.

only the active or circulating monetary funds can act on the volume of production and the price level, and that variations in the volume of hoarding, or in the financial circulation, are to be compensated by corresponding variations in the stock of money. Therefore, we start the analysis with a variation of the money stream, regardless of how it is caused.

The expression "constancy of the money stream" is, however, ambiguous. There exists, first, the so-called income fund, i.e. the amount of money available to pay out the current monetary net income (the income stream) for an average income period. But even in a stationary state there is, besides transactions in consumers' goods, a steady monetary demand for replacement purposes. The volume of this demand, of course, depends on the division of the higher stages of production among a number of independent firms. In a vertically integrated economy, replacement would be provided for within the boundary of the single firm and no demand for producers' goods, expressed in terms of money, would appear in the market. In a non-integrated economy the funds for the purchase of these replacement goods are provided out of the capital of the enterprises, which contains a revolving business fund; this fund is steadily depleted by purchases (and thus its resources are ultimately commuted into income payments) and it is steadily filled up out of the receipts of the entrepreneur. The relative size of this revolving business fund in comparison with the current net product, in an arbitrarily selected time period, depends on the extent to which the productive process is divided among different firms and on the average period of production, measured in the same time unit. The absolute size, in terms of money, depends also on the general price level. In this respect alone the effects of voluntary and of forced saving are necessarily different, since by forced saving the price level will be raised, and will in the new equilibrium situation be definitely above the price level in the previous equilibrium position. But the physical volume of producers' goods demanded for replacement purposes would evidently be the same in both equilibria. *real*

On the other hand, as soon as we pass from a static state to a developing economic system, evidently the revolving business fund will not remain the only source of demand for producers' goods. In this condition a part of the net income is saved and consequently a part of the income fund, the stream of savings, is also devoted to the purchase of capital goods. The situation becomes even more complicated if we introduce the fact of forced saving; for the additional credits granted to certain entrepreneurs are used, long before they reach the income fund, for the purchase of capital goods, but they represent neither the business fund, in the strictly static sense of a revolving fund, nor, of course, the income fund. It is probably this complication that led Hayek to advance the proposition that any decrease in this "stream of forced saving" will diminish the stock of capital, or as Hayek prefers to say, "shorten the period of production." In the next section we shall examine this proposition from the viewpoint of the structure of production. Here we analyze merely the monetary side. It goes without saying that any decrease of the current stream of saving, other things being equal, brings about a decline in the demand for producers' goods. This is true for the decline of voluntary as well as of forced saving. But a mere curtailment of the demand for producers' goods on account of less savings would obviously leave the business fund unimpaired, and thus replacement would not be hindered nor the stock of capital diminished. Hayek, however, seems to maintain that in the case of forced saving the price fluctuations eventually cause a diminution also of the revolving business fund.¹

It is easy to show that, from a purely monetary viewpoint, forced saving might result in a new equilibrium position. In the first phase additional receipts for the entrepreneur are created by rising prices with income payments stationary. Not the whole addition, however, can be considered by the entrepreneur as spendable. It

¹ The whole argument of Lecture II in *Prices and Production*, especially on pp. 51-7, is based on the confusion of the savings stream with the business fund. Hayek concludes (*cf.*, for example, German edition, p. 59) that a reduction of the demand for producers' goods brings about a retrogression to a less capitalistic structure of production, i.e. a destruction of capital.

becomes necessary to increase the revolving business fund in order to purchase at rising prices the same physical volume of raw materials and semi-manufactured goods. After a while the increased net receipts gradually diminish in consequence of rising income payments and a new equilibrium is reached, when the business fund as well as the income fund has become adjusted to the new price level, leaving the rate of entrepreneur profits, if any, at the old equilibrium level. Since, however, the period of production has been lengthened, the business fund will have increased more than the income fund. The task of the entrepreneur here is certainly not less easy than in the case of voluntary saving. On the contrary, it is much more difficult in the case of voluntary saving to accomplish the redistribution of the money stock because, with a given money stock, in order to provide the additional business fund, the income fund must be curtailed and the income rates must be subjected a second time to reduction, after having been reduced on account of the employment of more factors of production with a given income fund.

III

Fluctuations of Savings and the Structure of Production

From the foregoing analysis we may conclude that only through an analysis of the changes in the structure of production brought about by variations in expenditure can we evaluate the alleged dangers of an increase of the income stream. The dangers of a credit expansion were indeed well known to the earlier writers on business cycles. They were not only well known to the so-called monetary theorists like Wicksell and Mises, but they were especially stressed by leading German theorists like Spiethoff and Lexis. The main argument is quite simple: because every credit expansion is bound to stop at a certain point, forced saving must likewise come to an end. This becomes more evident when we consider that the rise of commodity prices and ultimately of income rates rapidly reduces the real magnitude of the forced saving fund. But does this

- > necessarily involve a shortening of the period of production, or to express it in a simpler way, a destruction of capital?¹

It is hardly necessary to stress again the distinction between a real consumption of capital and a mere diminution of saving. That
> any increase in saving means in itself a lengthening of the period of production or an increase in the capital stock, is true only if one may disregard the necessary production period of the additional capital goods and thus may identify the act of saving itself and the corresponding production of additional capital goods with the definite investment and putting into function of these additional goods. This may be permissible in certain circumstances, but it is simply not true that any "relative increase in the demand for consumers' goods brings about a shortening of the period of production." A diminution in saving even to zero is not under all conditions identical with the diminution in the stock of capital, but may mean only a decrease in the current increment of the stock.

There exist, of course, special circumstances under which a decrease in saving might impair even the stock of capital. We refer to the fact of a certain immobility of the real capital already invested.² A certain amount of invested capital may be destroyed if income receivers make changes in the disposition of their income, especially also if saving is displaced by spending, because a readjustment of the productive resources is only imperfectly possible. This fact is well known and it should not be minimized; one may freely admit that it may serve as a basis for a theory of business cycles. But it does not suffice to justify Hayek's criticism of every increase of the income stream, except in the case of a growing population, nor to prove that in the case of immobility, capital destruction is the inevitable outcome of credit expansion.

The following important qualifications must not be overlooked:

1. Any theory that is based on partial immobility of invested capital is essentially a frictional one. From this simple considera-

¹ In respect to this identification, cf. the Appendix to this article.

² Interpreted by Hayek in *Prices and Production*, Lecture III, where he introduces the distinction between specific and non-specific means of production.

tion it follows at once that the whole argument fails if we assume that the decrease of saving, however close to the zero point, goes on with the necessary slowness.

2. If this main feature of the argument is not clearly perceived, it becomes impossible to explain why, in the case of *less* saving, variations in the disposition of income exercise an effect on the stock of capital and the entire business situation which is quite different from the effect in the case of *more* saving. An increase in forced saving, which characterizes the starting of a boom, would destroy capital invested in the consumers' goods industry; a decrease in forced saving at the end of the boom would destroy capital invested in the capital goods industries. Why does the former type of destruction of capital start a boom whereas the latter type stops it? Or is Hayek justified in neglecting entirely the destructive effect in the first case and in looking here only to the ultimate effects of more saving on the stock of capital? Only three answers are possible: first, real capital per head may be much less in the consumers' goods industries than in the producers' goods industries; second, the assumed increase in forced saving might go on at a much slower rate than the assumed decrease; third, in the first stages of revival credit expansion might be able to utilize unused capacity of factors of production. The third answer, although the most realistic one, is not compatible with the starting point of the analysis, a system in full equilibrium. The first and second answers show clearly the frictional character of the whole argument.

3. Nothing in the whole analysis justifies the sharp distinction between fluctuations in voluntary saving and fluctuations in forced saving, which Hayek supports only by the argument from the demand for capital goods, which we have refuted in the last section. Evidently it is not a question of the character of saving, but of the tempo of its fluctuations. It may be readily admitted that in an epoch of unregulated credit expansion fluctuations in forced savings are much more likely than fluctuations in voluntary savings. This does not prove, however, that every regulated credit expansion would be subject to the same objection. Indeed, the

postulate of a smooth handling of the credit mechanism is one of the oldest elements of a scientific credit policy.

4. That credit expansion and forced saving will not inevitably be followed by capital destruction, is now admitted by Hayek in his article in *Econometrica*, quoted above. A destruction of capital followed by a crisis can occur only if, by a premature decline in saving, the structure of production becomes "uncompleted."¹

Since the consequences of this distinction reach much further than Hayek supposes, it is necessary here to elucidate them in a special section, in which a partial immobility of capital is assumed.

IV

The Case of Immobility

Incompleteness of the structure of production may mean three different things:

1. If, by saving and partial adaptation of factors of production, additional equipment is provided for a plant, it is necessary to provide also, according to the length of the period of production in this individual plant, an additional amount of working capital (goods in process).

2. If the commodity to be produced in this plant is not an entirely finished consumers' good, but itself an instrument of production, it is necessary to provide money capital for the purchase of this good, for additional working capital at the next lower stage, and so on down to the lowest stage of production.

3. If, by saving, the productive capacity of some of the higher stages for the creation of new instruments of production is increased, a current stream of savings large enough to take over the current output of additional instruments of production, beyond the mere replacement, is indispensable. A static equilibrium is restored only if the additional equipment at the lower stages has grown so large that the additional capacity at the higher stages,

¹The distinction between a completed and an uncompleted structure is already introduced in a short paragraph of *Prices and Production* (p. 53), but the rest of the book is not brought into harmony with this qualification.

created by the original investment, is just sufficient to secure replacement for the lower stages and leaves no margin for additional investment.

It follows that, to avoid incompleteness of structure, saving must not be decreased by more than a certain amount, as indicated by the foregoing analysis. Hayek's determination of this amount, however, is not correct: "As long as the supply of capital does not decrease by more than the amount which has so far been used to construct the new plant making that equipment, there is no reason why the demand for new equipment should fall off."¹ First, it is not permissible to use the magnitude of a certain stock of capital for the determination of the size of a current time stream, without regard to the length of the time period. Second, since in starting a new roundabout process the whole additional supply of capital is devoted to the construction of a new plant, Hayek's criterion would permit a falling off in saving to zero, quite contrary to his main idea. This is true only if the structure is completed, in the sense of point 3 above. So long as a new equilibrium is not reached, the indispensable amount of saving is determined by the current net output of capital goods, beyond mere replacement, that is due to the original additional investment; the size of this current stream depends by no means on the size of the original investment alone, but also on its rate of turnover.

It is necessary to assume not only that the amount of saving does not decrease too quickly, but also that it does not decrease too slowly, if the equilibrium between supply and demand of goods is to be preserved. If the structure of production is really "completed," in the sense of point 3 above, a supply of additional capital goods no longer exists; therefore if saving does not drop down to zero, only a new adaptation of the productive resources could preserve equilibrium and in this stage of the argument such adaptation is to be disregarded on account of the partial immobility of the capital. Or to express it otherwise: the process of completing the structure of production is one which takes place within a defi-

¹ Hayek, "Capital and Industrial Fluctuations," *loc. cit.*, p. 150.

7
When ?
nite period of time, since eventually, as indicated above, the additional plant erected through the original act of saving (voluntary or forced) will in its whole capacity need replacement. Down to this point the produce of this plant, representing producers' goods, had to be bought out of savings of some kind; with the maturity of the process they come to be purchased out of the revolving business funds which have come to be established at the stages of production between the consumers' borderline and the stage of the original investment. In so far as immobility of capital prevents the adaptation of the productive apparatus to a changing structure of demand, whether shifting from saving to spending or from spending to saving, forced saving must run through a half cycle from zero to zero, if capital destruction and unnecessary disturbances of business are to be avoided. A deviation from this middle path would cause a crisis from capital scarcity or underconsumption.

v

Non-Static Conditions: Depression

We readily admit that it would be very difficult for the credit authorities to keep strictly to this sound line of credit expansion, not only because they would completely lack adequate knowledge of the empirical conditions, but above all because they would lack efficient means of control, since in times of violent profit changes the influence of both discount policy and open market operations is very restricted. In so far Hayek's warning is entirely justified, although the theoretical basis of this warning is not sound. His application of a static analysis to non-static conditions is, however, not justified. Two types of non-static conditions require a closer examination: the later phases of a depression, and an expanding economy characterized by an increase of a single factor or of several factors of production. As to the first, Hayek opposes even a reflationary program in his recent article, and would hardly admit it even if "the expectation of a further fall in prices has led to hoarding."¹ But if, by a general deflationary process, unemploy-

¹ *Loc. cit.*, p. 163.

ment of all factors of production is brought about (contrary to Say's law of markets) and even working capital, in the form of stocks, is abundant, an increase in the money stream cannot have the same effect of forced saving as it would have under strictly static conditions. No rise of prices, no forced saving at all would occur; the various idle factors of production would be assembled and made active through provision of the necessary cash; the increase of current income would be accompanied instantaneously by an increase in the current net output.

VI

Non-Static Conditions: An Expanding System

This case, however, is from the viewpoint of general monetary policy rather less interesting, since here a definite phase of depression is assumed, which might not have occurred at all if the preceding inflationary credit expansion had been avoided. In the second case, in which the supply of factors of production is assumed to increase as a result of the growth of population or of voluntary net saving, a double difficulty arises. On account of the rigidity of income rates, a constant money stream would bring about dangerous deflation and an increasing money stream would, according to Hayek, produce dangerous inflation. We cannot, of course, accept this latter view. If the credit expansion were restricted to the satisfaction of the additional monetary demand for income payments, arising out of an additional supply of the factors of production, and for an increase of the business fund, if any, neither a rise of prices nor a rise of profits (the source of forced saving in the foregoing analysis) would occur. Forced saving could then mean only that the consumers are deprived of the advantage otherwise to be obtained from a falling price level, an advantage which, however, assuming a constant money stream, would accrue only to the receivers of fixed incomes and even to these only down to the bankruptcy of the debtor.

This will become clear if we consider the instance of a proportional increase of all factors of production, without any change

in technique. The economy would expand through the erection of new plants in which additional labor would find employment. During the initial period of production the equipment of these plants and the income payments to the capitalists who have supplied the capital and to the laborers employed would have to be financed out of voluntary savings. But at the moment when the produce of these new plants, which may be assumed to be characterized by a diversification corresponding to the composition of the produce of the economy as it existed before the increase under discussion, reaches the consumers' borderline and has to be sold, it would become necessary to provide the new income receivers (capitalists and laborers) with additional purchasing power; in the same way the new enterprises themselves would have to be provided with the necessary business fund to operate the turnover at the different stages. The assumption of a constant money stream requires, obviously, that these funds should be drawn from voluntary saving; but this would deprive the old enterprises of some part of their necessary funds, income funds as well as business funds, and would thus prevent the income receivers from buying back the produce of these industries at the old price level. Deflation, i.e. a general decrease of income rates, of commodity prices and of the business fund, would be required to restore equilibrium on a lower price level. To avoid these monetary disturbances it is likely that Hayek himself would admit the expediency of a monetary expansion. But exactly the same considerations lead to the conclusion that in the case of a one-sided increase of only one factor of production, e.g. of the stock of capital, it would be possible to avoid both deflation and inflation if additional money funds were created for the financing of additional income payments (interest payments, and with a rising marginal productivity of labor, wage payments) and of the additional business fund, on account of the lengthening of the period of production.¹

¹ Hayek allows such an increase of the money fund only if the business sphere is relatively increased by growing differentiation, holding that when the increase is due to capital investment monetary expansion would necessarily be followed by an eventual shortening of the period of production, i.e. by destruction of capital.

We have already pointed out that an increase in the monetary income fund is due only after the conclusion of the initial period of production,¹ at the time when additional consumers' goods are to be sold. Income payments during this first period have to be financed out of voluntary savings; they are represented on the left side of the enterprise's balance sheet by a stock of working capital, i.e. real commodities, whereas at the end of this period an income fund consisting of newly created money which is to be paid out at the beginning of the next period appears as a new asset. The increase of the business fund must commence at an earlier stage, when it is necessary to make the first turnover of the additional output at the successive higher stages of production, organized in independent firms. In the existing system the increase in the income fund is determined by the amount of additional income created during one average period of income payment, while the increase in business fund is determined by the amount of the additional turnover at the higher stages, divided by the velocity of circulation in the sphere of business.² This may be illustrated by a simplified example. Suppose a degree of differentiation equal to zero, i.e. no business fund at all, and a single investment of new capital not followed by other investments. At the close of the initial production period of, say, thirteen weeks, the additional produce evidently represents the subsistence fund for the additional workers and capitalists in the next thirteen weeks and has to be bought back out of their income. If the income period is uniformly one week, an additional income fund equal to one week's wages and interest payments suffices to operate these purchases; because during the week the income fund, paid out at the beginning, will, other things being equal, flow back to the entrepreneurs and be paid out again to workers and capitalists at the

¹ "Period of production" means here the period of the creation of working capital within an enterprise, as distinguished from Böhm-Bawerk's period of production, the length of which is determined also by the volume and the lifetime of the fixed capital.

² Cf. the closer analysis in my article, 'Kreislauf des Geldes' in *Weltwirtschaftliches Archiv*, vol. xxxiii (1931), p. 369 ff.

week's end, and so on indefinitely, since the assumed production process is continuous.

If we keep in mind the existence of these particular monetary components in the total capital of the enterprise, we are also able to answer the question, why the lowering of interest rates by credit expansion does not cause a deviation from the equilibrium position in the demand for capital goods and in their price level. These new monetary components do not directly add anything to the marginal products of the real capital components, but they are entitled to draw their interest out of the receipts of the enterprise just as the real capital is entitled to draw its interest;¹ therefore the marginal productivity of the increment of total capital is less than the marginal productivity of the increment of real capital. By a corresponding lowering of the supply price of capital, equilibrium is restored. On the one hand the savers have to share the total interest earnings with the banks that grant the additional credit; on the other hand, the demand for capital goods is represented only by a part of the new investment, and is just as it would be in a barter economy.

A monetary expansion as proposed by this scheme would stabilize the average commodity price level, so long as the increase in the physical volume of production is due only to the increase in the volume of the factors of production. This scheme would not apply in cases of purely technical progress, in which an increase in the physical volume of production occurs without any increase in the factors of production and consequently without any increase in monetary costs for the entrepreneur. In this case stabilizing the price level would result in temporary additional profits of an inflationary kind, as maintained by Hayek, who also erroneously applies the same reasoning to a lengthening of the period of production. We shall not dwell at length on the different detailed problems that arise out of our rejection of the general idea of price stabilizing in cases of technical progress, and out of our acceptance

¹ We assume here, for the sake of simplicity, a supply elasticity of savings equal to zero; the argument, however, remains substantially true if we substitute a positive supply function.

of the idea of stabilization of the average income rate as the most rigid element in the whole system. This is discussed sufficiently elsewhere.¹ We have sought only to show that there is a safe middle path between inflation and deflation and that in this case none of the dangerous consequences, alleged by Hayek to follow any monetary expansion whatsoever, would arise.

This is the true "neutral money," the money which permits our monetary economy to behave exactly like a barter economy. Income rates will be changed only if the relative marginal productivity of the factor changes and not merely on account of the growth of the whole system, as is assumed in the case of Hayek's constant money stream.² In the monetary economy as well as in the barter economy, the basis for increasing production, namely, the stock of real capital (fixed capital and working capital), must be provided for by voluntary saving. But the monetary economy differs from the barter economy in so far that in the former revolving money funds (the income fund and the business fund) are needed for the operation of the turnover of goods. What is more natural than to make good this difference by providing these additional funds and creating additional money in all cases if the number or the size of the enterprises, on account of a growing supply of factors of production, is increased?

VII

Some Applications

The application of this rule for monetary expansion would necessarily cause a secular downward trend of prices on account of genuine technical progress. The real price trend since the beginning of modern capitalism has shown the opposite direction. We cannot but conclude that the whole period has been characterized by tendencies of inflationary expansion, which, however much they may have contributed to the accumulation of capital by forced

¹ Cf. Haberler, G., "Die Kaufkraft des Geldes" in *Schmollers Jahrbuch*, vol. iv (1931), p. 993 ff.; Egle, W., *Neutrales Geld* (Jena 1933); and my article "General Overproduction" in *Journal of Political Economy*, vol. xlii (August 1934).

² For Hayek's and Koopmans' concepts of "neutral money," see Appendix, section II.

saving and facilitated the realization of technical progress, must necessarily, on the other hand, have accentuated in times of prosperity, as well as in times of depression, cyclical movements in the course of capitalistic growth. In the second half of the nineteenth century, according to the famous Cassel-correlation, the supply of gold was large enough on the average to maintain general commodity prices on the same level as at the beginning. We must therefore consider this period as one of true gold inflation, which without doubt is partly responsible for the recurrence of crisis and depression, although we should by no means consider crises as caused exclusively by monetary events. Cassel and his adherents foretold for the postwar period a decline of prices on account of a rate of increase in gold smaller than the rate of increase in the net product, but this fact should not, in our opinion, be considered a disadvantage of the gold standard, but rather as an opportunity to avoid at least monetary disturbances like those of the past.

The question arises whether regulation of the volume of credit, as suggested here, could be accomplished only by an active policy on the part of the central bank, or whether the traditional rules of commercial banking suffice to regulate the volume of bank credit and deposit money, according to the principle indicated above. Naturally we do not intend to discuss the whole set of problems raised by this question. We restrict ourselves to an examination of the relation between the income rate standard as here defined and the old banking rule, according to which only the working capital of the economic system, or a part of it, should be financed by short term obligations of the banks. We assume that this rule is strictly followed, i.e. that the period of the additional credits granted by the banking system is just equal to the average production period of the working capital (or of a definite fraction of it), so that the total value of this working capital would be equal to the total amount of short time liabilities of the banking system. It goes without saying that this equation holds true only of the system as an entirety, not of the financial status of a single enterprise; if one industrial enterprise prefers to do without the aid of

bank credit, the lack of purchasing power caused by that rather puritanical financial method could, for the whole economy, be compensated by an overissue of bank credit to another enterprise.

It is obvious that the equivalence of the income rate standard and the working capital standard could not be determined by theoretical deduction, but only stated as an empirical (and in so far accidental) equality of different magnitudes in the economic system; because the increase of working capital, excluding in this case its merely monetary components, depends on the volume of saving and on the share of working capital in the total amount of capital, which is determined by merely technical factors. On the other hand the increase of the income fund as required here depends, first, on the rate of increase of factors of production; second, on the relative share of these factors in the net product; and third, on the average income period. The increase of the business fund depends on the velocity of circulation in this sphere and on the rate of increase of the total capital stock.

Generally speaking, it cannot be doubted that the stock of working capital in a modern economy is much larger than the stock of money, and, *a fortiori*, larger than the income fund plus the business fund, which represent only about one half of the total money stock, the other half consisting of emergency hoards (carryover from one income period to another) and financial circulation. To express it otherwise: the velocity of turnover of working capital is much slower than the average velocity of turnover of the income and business fund. What is true for the existing stock is also true for the increments, a minor qualification to be mentioned later.

For an exact statistical analysis we lack the necessary material. It might be useful, however, to give an idea of the order of magnitudes, and to determine in this way the fraction of working capital than can be safely financed by additional banking credits. One has to keep in mind that, in principle, the result does not depend on the assumed magnitude of the different factors, except as to the relative velocities.

As representing the stock of working capital we may use the

statistics of commodity stocks. This does not include buildings in process; this, however, may be justified by the fact that they usually do not represent a basis for short term banking credit. Consequently if the composition of additional investment should change by investing less in residential buildings on account of a declining growth of population, the relative share of working capital in this narrower sense would increase. On the other hand, there is included in the statistics of stock commodities also the so-called "liquid capital," i.e. speculative stocks, which, however, represent in most cases a basis for banking credit. The amount of commodity stocks is usually indicated as between a third and a half of the annual net product; supposing a stock of total capital six times as large as this annual net product, working capital will represent between 5 and 10 per cent of the total capital; for the sake of the argument we will use the lower figure. The lower and upper limits of the savings quota, in relation to net product, might be fixed at 10 and 20 per cent. On the basis of the working capital standard, there will thus be created an additional money fund equal to 0.5 to 1.0 per cent of the net product.

Analyzing now the effects of the other standard, we have to consider first the increase of the income fund. The relation between earned and unearned income may be assumed today as 2:1; we disregard the possibility of great changes in the relative marginal productivity of factors, which would, of course, alter that relation. The supply of labor grows in the long run at a rate corresponding to population, i.e. at an annual rate between 1.5 per cent and zero. The stock of capital increases according to the assumptions above between 1.7 and 3.3 per cent per annum. Taking first the higher figure, the average income fund ought to be increased between 1 and 2 per cent, according to the rate of growth of the population. The increase of the business fund must be put slightly higher, because it is closely correlated with the increase of the capital stock; but since the business fund is much smaller than the income fund, if we exclude mere emergency hoards and the financial circulation, the upper limit for the average rate of increase of the total money

stream, as required by the income rate standard, could be put between 2 and 2.5 per cent of the existing funds. These existing funds, income fund and business fund added together, represent only about a half of the total monetary stock and are equal to about one eighth of the annual national income. The income rate standard requires therefore an increase of the monetary stock equal to between 0.25 and 0.3 per cent of the net product, whereas the working capital increases about 1 per cent per annum. If we take the lower limits for the increase of capital, there is required an increase of the money stream of 0.2 per cent (with a population rate of 1.5 per cent per annum), or about 0.1 per cent (with a stationary population) against an increase of the working capital of about 0.5 per cent. It must be admitted that some part of the newly created money will be diverted into emergency hoards or the channels of financial circulation. But, since this is done by saving and the existing stock in both these spheres is built up out of the savings of generations, the figures elaborated on the basis of the income rate standard have, for the time being, to be increased only slightly.

We cannot but conclude that the working capital standard is more suitable for price stabilizing than for the stabilization of income rates. By cutting down, however, the financing of working capital by bank credit to about 5 per cent of its value, the dangers of inflation would be almost wiped out. This restriction would be important for the postwar period even more than for the prewar period, because the postwar period is characterized by a declining increment of population which lowers the rate of monetary expansion required by the income rate standard, and, as indicated above, raises this rate as provided by the working capital standard. In any case, the dangers would be diminished by the fact that a relatively large share of the working capital is usually provided out of voluntary savings. But the necessity for a stricter control of credit expansion can, in our opinion, no longer be disputed.

The Average Period of Production

In the text we have used the customary concept of the rate of turnover of capital (stock of real capital divided by the value of the net product) as equivalent to the concept of the average period of production that was introduced by Böhm-Bawerk and is defined by him as the sum of the labor costs of the (net product) weighted by their respective time-distances from the consumers' borderline, divided by the labor value of the net product. Hayek, too, treats both definitions as equivalent. This is correct for a stationary state, is *prima facie* probable, and now proved mathematically by Dr. Marschak.¹ Evidently this rate of turnover can vary only if the numerator of the fraction changes, i.e. if the stock of capital is increased or decreased, or if the denominator changes. This latter change can occur, first, if the marginal productivity varies on account of technical progress, which is excluded by our assumptions as well as by Hayek's, or second, if the productivity functions in different trades are different and a redistribution of productive resources occurs on account of more or less spending; this effect is only of the second order of magnitude and may be neglected. We are, therefore, justified in identifying a shortening of the period of production, in Hayek's terminology, with a destruction of capital, and vice versa.

As long as one uses the customary concept of the period of production, one cannot be tempted to identify a mere diminution of saving with a shortening of the period of production and a destruction of capital. But if one uses Böhm-Bawerk's definition this danger is very great, as shown by the example of Hayek, because more saving seems to cause a shifting of productive resources to higher stages, and less saving a shifting to lower stages; according to Böhm-Bawerk's formula the period of production is affected

¹ Marschak, J., "A Note on the Period of Production" in *Economic Journal*, vol. lxiv (March 1934).

by these shiftings, which alter the time-distances. The solution of the puzzle lies in the simple fact that the equivalence between both formulae for the period of production does not hold good under non-static conditions. One may doubt whether one can measure time-distances from the consumers' borderline within an uncompleted structure of production and thus apply Böhm-Bawerk's formula at all in this instance. But if one does, surely the conclusion is no longer justified that changes in the average period of production are identical with increases or decreases of the stock of capital.

We shall not dwell at length on the complications of Böhm-Bawerk's pattern of stages of production, which underlies the concept of the average period of production. Amended in a certain way to correct some mistakes, it may in our opinion serve as a useful scheme of the structure of production. Two misunderstandings of Böhm-Bawerk's must, however, be noted here briefly, because they concern the term "average period of production" itself. First, producing with a higher capital quota per head is identical with a lengthening of the period of production only if and when the law of diminishing capital returns is in force. Second, the difference between the average production period and the average waiting period is not altogether clear; Böhm-Bawerk seems here¹ to have confused the former concept with the period that elapses between the "starting" of a production process and the final completion of the produce.

II

Hayek's and Koopmans' Concepts of "Neutral Money"

The question, what monetary system may properly be called "neutral," is essentially a question of terminology. But because terms are chosen not without reasons, it may be worth while to examine in brief the meaning attributed to this term by Koopmans² and

¹ Böhm-Bawerk, Eugen von, *Positive Theorie des Kapitals*, 4th ed., vol. i (Jena 1921), p. 119 ff.

² Koopmans, Johan G., "Zum Problem des 'neutralen' Geldes" in *Beiträge zur Geldtheorie*, ed. by F. A. Hayek (Vienna 1933), p. 214 ff.

by Hayek himself. The common starting point is the definition of "neutral money" as the monetary system that minimizes the differences between a barter economy and a monetary economy. From this viewpoint Koopmans restricts the creation of additional money to compensation for hoarding (keeping constant the total money stream: income fund plus business fund) in order to avoid the creation of a "pure demand"; whereas Hayek, as mentioned above, would increase the business fund on account of an increasing differentiation, but not on account of an increasing stock of capital. In this respect, however, no satisfying comparison between the two economies is possible; for one cannot imagine a barter economy with a vertically differentiated structure, because intermediate goods cannot be produced for the market if there does not exist a general unit of account or of value.

On the other hand, both Koopmans and Hayek overlook one main difference between the two economies, namely, that in the barter economy all contracts are fixed in units of real goods, and, in a monetary economy, in money. In the former costs represent, therefore, always a certain amount of goods: in this respect the barter economy is obviously close to a monetary system with a stabilized price level. By adopting the monetary policy defended in the text above, this important difference between the two economies may be virtually wiped out; and in the same way it is possible to avoid the dangerous influences on the structure of production that are shown by Hayek for the general price stabilizing projects, and which have led him to an almost universal rejection of any monetary expansion.

Koopmans supports his analysis of "neutral money" by a criticism of the traditional quantity theory. In his opinion, the so-called "law of compensatory price variation" (according to which, other things being equal, any variation in the price of one commodity is compensated by an opposite variation in other prices) is true only in the case of a demand elasticity of less than unity; in the case of $\nu > 1$ the effects on the rest of the price system are said to be "cumulative," and in the standard case of $\nu = 1$ he denies any effect

whatsoever. Obviously, the meaning of the formula "other things being equal" is misunderstood by Koopmans. Not only the supply (or turnover) of goods in the rest of the system,¹ but the total supply, is supposed by the quantity theory to be constant, if the law of compensation is to hold good. But in the standard case of $v = 1$, for example, any lowering of the price is correlated with a proportional increase of the turnover of the good concerned; therefore either the total turnover of goods is increased and the decline of the general price level caused in this way, or productive resources are withdrawn from other uses, which must cause a rise of prices in the branches concerned and bring about a compensation of the original price decline.

The result is not surprising: if the basic equation of monetary theory is, as usually asserted, a tautology, it cannot also be wrong.

¹ Cf. *loc. cit.*, p. 297: ". . . bei unverändertem Angebot der sonstigen Güter . . ."

THE INTELLECTUAL ORIGINS OF FASCISM

BY G. A. BORGESE

THE first and second rules of reasoning, as formulated by Newton and repeated by popular physicists down to the present, read as follows: "We are to admit no more causes of natural things than such as are both true and sufficient to explain their appearance. . . . Therefore to the same natural effects we must, as far as possible, assign the same causes. As to respiration in a man and in a beast; the descent of stones in Europe and America; the light of our culinary fire and of the sun; the reflection of light in the earth, and in the planets." Such rules are valid for human as well as for natural history, and therefore the reasons that explain Italian fascism must be good, at least in their main outlines, for German fascism too, and vice versa, or they are not reasons at all.

Attempts have been made, both from the political and from the economic approach, to establish the fundamental character of this new type of political organization. It has been said that German fascism is a revolt against the injustices and humiliations of the Treaty of Versailles, a revulsion of defeat. But this interpretation does not account for the birth of fascism in its country of origin, Italy, a country which had won the war more smashingly than any other of the combatants, utterly destroying her hereditary enemy, the Austro-Hungarian monarchy, and acquiring a frontier of a perfection, geographical, ethnical and military, unparalleled in continental Europe. To be sure she failed in getting hold of that zone of the Dalmatian mainland, opposite to her coast and inhabited almost wholly by Slavs, which the Allies had formally granted her; but she won Fiume, which she herself had promised to Croatia, and she took definite possession of Rhodes and some other Greek islands off Asia Minor, of which her occupancy had hitherto been considered more or less temporary. It is also true

that she did not share, as largely as her sacrifices entitled her, the tough and bony African and Asiatic prey, improperly although magnificently called the "colonial booty." In this she suffered a disillusionment partly due to the selfishness of her partners and partly to her own lack of colonial purpose. Also she felt that England and France were blindly stubborn in contesting with her even some ragged readjustments of borders around her sandy or rocky African territories. But such minor failures, even supposing that they injured real interests more than feelings of pride, cannot make a defeat out of a victory. Neither can they justify the nationalistic slogan, "Italy won the war and lost the peace." Among some Italians a feeling of defeat arose and gradually increased during the years 1919 and 1920; but it was a matter of feeling, not of fact, and it was a consequence, not a cause, of the fascist and pre-fascist mentality which later swept the country. For their emotional purposes these Italians wanted a feeling of distress, and they got it.

Happy warriors, totalitarian victors, exist only in the jealous imagination of competitors or, less frequently, in the case of nations as well as in that of individuals, in the self-sufficiency of a delicately balanced and moderate mind. If the imperfection or, as it was said, the mutilation of the Italian victory explains fascism, why had not fascism risen earlier and elsewhere, after other partially unsuccessful victories? Why did it not rise immediately after 1918 in France, who had lost both the main issues of her victory as conceived not only by inflamed nationalists, but even by cautious patriots, and was unable to get either the Rhine frontier or the Anglo-American guaranty of her safety? Why did it not rise in England, who saw, as an indirect but prompt consequence of the triumph, Ireland drifting away and the ties of the Empire loosening? Or even in America, which did not acquire any territory worth mentioning and, rather stunned, lost her money? This is indeed no world of justice, no Kingdom of God; and the destiny allotted to the Italian nation, jammed as it is in a poor and narrow territory, is inferior to the claims she may base not only on her historic grandeur but on the actual ambition of her living children to

collaborate in the work of human civilization and to pluck, also, some deserved fruits of human happiness for themselves. But even admitting that this feeling of inferiority was bound to grow more insistent after the passion and sacrifice of war, and in spite of its positive results, why did it find its expression in fascism and not in a subspecies of communism or, as reason seemed to suggest, in a political plan which would somehow have made Italy the leading power in Geneva?

Italy was, as she is, the strongest among the feeble and the feeblest among the strong. Her universal background and ambition might have gained for her the position of leader of the minor and proletarian nations of Europe, to balance with their help the "Mighty of the Earth," opposing the great powers when necessary and pushing them toward a sincere submission of their shrewd policy to their lofty principles. Italy might have made it her mission to revive the inspired democracy of Mazzini, adapting it to changed circumstances; to translate into European concreteness the idealism of Wilson; to quicken the pace of history toward the next goals: a federation, political and economic, in Europe, and a consortium in the colonies, with the "open door" and equality of rights. Certainly such a role would have been much less appealing to particularistic vanities, but proportionally more satisfactory if the aim were real justice and — why not? — real business. This plan might have been conceived, and it was indeed conceived by some Italians of those days; it was, or seemed to be, at the same time wise and great. Perhaps it might have won the support of America, but it did not please the Italian mind and heart of those days. Not only did it appear utopian to the mind; much more important, it was distasteful to the heart. And fascism came.

What Walter Lippmann wrote about Russia and America is equally true for Italy and Germany, and for any country at any time. "It is certain that men must eat; it does not follow that they can eat only what the cook chooses to provide. . . . It was certain that after the breakdown of Czarism there would have to be a new regime in Russia. . . . Yet it was not certain that it had to be the

regime of the Five Year Plan. That was the dinner the cooks happened to provide for hungry men. After the collapse of 1932-1933 a New Deal of some sort was imperative. But not everything that has been dealt out was imperative. That has depended upon the temperament, the prejudices, the quick judgments of the dealers."¹ There was no Italian defeat, and there is no reason to believe that defeat, either imaginary or actual, either Italian or German, had to be followed by fascism. Turkey and Russia were severely and unmistakably defeated, but they resorted to Kemalism and communism, which were indeed dictatorships, but of quite a different brand from fascist dictatorships.

What matters, in each of these cases, is the mental and sentimental background of "cooks and dealers."

It is even easier to dispose of the purely economic explanations that are customarily given of the phenomenon of fascism.

Marxism, at least as a prophecy, collapsed long ago; so everyone asserts. But Marxian concepts and formulae still hang, each on its peg, in the wardrobe of popular mental apparel. They are comfortable and ready to wear. Hence the interpretation of fascism as the angry self-defense of capitalism against the communistic and socialistic menace. But why then did it not appear in Poland or Rumania or the other states bordering on Bolshevism; why did it not appear in France or in any other country where capitalism is really strong and socialism is more or less militant? It is not a simple matter to explain, on purely economic grounds, why the chosen land of fascism, its Mecca or Bethlehem, had to be Italy, where capitalism was comparatively weak, and where in 1922 an agonizing socialism, which had never been very much alive, expressed what strength it had only in rhetorical strikes, compared to which the recent events in San Francisco and Minneapolis or in the American textile strike could be considered as full fledged revolutions.

The answer usually given is that *because* capitalism was weak,

¹ Lippmann, Walter, *The Method of Freedom* (New York 1934) p. 24-5.

it had to rely on violence; *because* socialism and communism, after some years of foolish threats, had proved ineffective, the time was right for revenge.

Another attempt at explanation which has recently become familiar is that the middle classes were impoverished in Italy, ruined in Germany; they had to start something. Why this something; and why was it they who had to start something, and not the peasants and workers? Were peasants and workers happy and wealthy in Italy and Germany? Or, again, the middle classes in Italy and Germany had had no sufficient experience of freedom; therefore they crushed it.

In other words: these middle classes were ruined, and they were victors; they were strong, and they were weak; they were strong enough to crush freedom and the other classes; they were not strong enough to compromise with the other classes and to maintain freedom.

All these may be truths. But they exhibit a quality of neutral, compensated, pendulum-like truth that has nothing, or very little, to say.

There certainly would be no fascism if the war had been followed by the miracle of a peace satisfactory to everybody. There would be no fascism if there had been no communism. Looking at a European map one visualizes a fascist trench or wall, a black stripe from Sicily to the Baltic shore, which in a way seems to protect the world of Western capitalism against the other world, the world of communism; it looks like a broad dike; or, to strain the right of metaphor further, it resembles a scar through which the capitalistic flesh reacts against the revolutionary wound. The existence of an outer zone, from the Balkans to Finland, does not impair the validity of the simile. These minor states, often also of very recent origin, are a softer surface on which an irritated reaction was less to be expected and would have been less definite.

A conception of this sort may appeal to the imagination and may contain, although symbolically, a part of the actual reality. A part

of reality is also contained in the views that emphasize the results, political or economic, of the war. But these are the crude materials of fascism; they are far from giving its specific nature and spirit. They explain that some kind of reaction might have occurred, or must occur, that the European body was bound to get a fever; they do not explain at all why and how and where that particular kind of reaction had to occur, why that particular kind of fever had to befall those nations.

For long centuries historiography was almost totally political. It dealt with treaties, with great men and their ambitions and beliefs. Then came the Marxist reform, and history writing became economics and the class struggle. If we want a more complete and truthful insight into human events, the intellectual and emotional elements of those events need to be taken more largely into account. They are not always economic interests in disguise; much more often, on the contrary, the economic interests are embodiments and materializations of intellectual judgments or prejudices and of emotional drives.

When the logical analysis has been pushed to its conclusion one realizes that the specific elements of fascism are of a mental and sentimental nature; they are the ideal and emotional backgrounds of "cooks and dealers"; and only through these, as through common denominators, is it possible to attain an interpretation of fascism and of its issues that is equally adequate for Italy and for Germany. Of course, these ideas and emotions embodied themselves in the political rivalry of states and in the economic class struggle; what happened first in the mind found its way into the facts of mass history. But it happened first in the mind.

This mental pedigree reaches far back. Included in it are Machiavelli and the Florentine historians of the Renaissance with their bitter contempt for the idealism of words and for unarmed prophets, and their elaboration of the concept of the state as might. Overlooking analogous tendencies in the Greek sophists, many were their forerunners among the writers of the early Renaissance. Croce

quoted complacently, many years before the fascist rise, the story of Messer Ridolfo da Camerino, as related by Franco Sacchetti. His nephew, after having studied law for twelve years at Bologna, came to visit him. He asked, "And what didst thou do at Bologna?" The young man answered, "My Lord, I have learned reason." Then Messer Ridolfo replied, "Thou hast spent thy time ill. Because thou shouldst have learned force, which is worth two of the other."

But, nearer to us and with an incomparably more decisive effect, we have, early in the decline of the eighteenth century, the German Storm and Stress, with its appeal to violence and passion and its uprising against reason and rule. Lessing, in his *Laokoön*, had opened the path to the wilderness, substituting in the appreciation of poetry passion and expression for the classical criteria of order and beauty, of "noble simplicity and calm grandeur." He had also most resolutely asserted that if man had to choose between the possession of truth and the research for truth, he should prefer the research; the effort is better than the goal — a proposition that included in itself much more explosive stuff.

The revolt, far beyond the conception of Lessing, was one against both classicism and Christianity. Naturalism and nationalism, primitivism and extreme individualism, hero worship and pessimism, all these ideas and others connected with them were born, so to speak, all together in a bundle at the very outset of the eighteenth century which, after having built up an intellectual system of reason, universality and human hope, distilled also the intellectual by-products whose slowly increasing accumulation was finally to overwhelm the results of the constructive work. Of course the intentions of the forerunners, often involuntary, did not always include the necessity of the consequences; Lessing and the *Stürmer und Dränger*, for instance, were inspired by a lofty desire for freedom and justice. But in the later disintegration of European thought this moral background was forgotten, and the nude appeal to violence and expression came to the fore.

Nationalism has proved to be one of the main ingredients of

fascism. In a way it is of course related to patriotism, to the selfish-unselfish, tender and proud feeling that obviously and almost instinctively attaches every human being to his native place, be it hamlet or metropolis, parish or continent. But in another way it is a feeling or emotion quite recent, and of a quite different quality, and inexplicable without the philosophic issues which it presupposes. One of them is naturalism. Assuming, as even Bergson assumes, that nature's purpose was to organize mankind in separate group formations, each eventually fighting the others (much the same as among some arthropods, especially ants), no doubt seems to be left that nations, as they appear organized in modern states, obey nature's purpose at its best. Their perfection, if it cannot be traced back to religious mission or to purity of race, lies in the unity and exclusiveness of language. Generally speaking, one may say that a nation is the realm of a (literary) language: an entity deeply significant for romanticism and its mystic worship of words. Whatever may be the partial origins that modern nationalism can trace to the ancient world and to Hellenism, comparatively few have realized that its pattern came, through the Bible, from the Jews: a group formation, ideological, racial and linguistic, unparalleled in its self-sufficiency and self-awareness, the real paradigm of any modern nationalism, especially German. This modern conception of nationalism pretends to be equally superior to the narrow exclusiveness of the ancient city or of the mediaeval commune, and to the abstract emptiness of internationalism and supernationalism. It has often been repeated that the individual and the universal find an unsurpassable dialectic synthesis in the idea of the nation; that this is the field where nature and reason meet. To overstep its boundaries into universalism, is not only utopian, it is unholy, because the nation is constituted by nature, and nature is holy.

At the root of this error is the romantic belief that nature is supreme, instead of being an environment whose opposition the human mind, if it so chooses, must overcome. If universalism is judged better, nature, or the imagined nature, cannot be strong enough to stand against the better choice of human will.

Another philosophic and emotional issue implied by nationalism is mere individualism. If an individual who lacks a feeling of superiority cannot attain it through his personal power or mind he can always have recourse to a collective device. He may fancy himself as belonging to the highest possible human group formation, and therefore a shareholder in this corporation of superiority. If the capital of the corporation is boomed, so also is his personal share. Indeed, for most people, this gain may be had in ordinary times with very little personal effort, and for the majority of intellectuals and politicians, who are often the most excited about national primacy, without effort or risk even in extraordinary times. This is the obvious connecting link between nationalism and egotism; an egotism more easily fed than any other kind, since any individual belonging to the chosen people, whoever he may be, is unquestionably chosen and superior from the moment of his birth. Nationalism and fascism praise themselves as authors of a new ethics of duty and hierarchy; but on the other side they start by conferring a birthright, and a big one, upon all the members of the nation, building out of it a totalitarian aristocracy, which is a synonym for demagoguery. There is a story of the Emperor Charles V who, before a little crowd of little noblemen greedy for advancement, lifted his right arm and jokingly decreed, "Estote comites omnes"—"I make all of you counts." The nationalist dictator on his balcony or podium, lifting that same arm before the big crowd, earnestly decrees, "Estote principes omnes"—"You are all chiefs."

In the melting pot of fascism are naturalism and individualism, as they are combined in the spiritual chemism of nationalism; neo-Machiavellianism and Storm and Stress; ideal of the totem and of the "folk" and hero worship (from Schiller's *Räuber* to the pioneers or even to the gangsters, and in the other direction from Plutarch to Napoleon and even to General Boulanger); aesthetic privacy of aristocratic feeling and herd-like compactness of demagoguery; operatic picturesqueness of conspiracies (from Ku Klux Klan onward) and equally operatic thrill of parades and processions;

appeal of the past and revolutionary thrill toward an unknown future; philosophic — chiefly Fichtean and Hegelian — “nationolatry” and statolatry; philosophic anarchism; and many other more or less romantic substances. Their prolonged enumeration would be as easy as futile: a matter of course, and a matter without end.

Indeed, the success of fascism among middling cultured middle classes and lower intellectuals is mainly due to the thoroughness and critical indifference with which it has made and still makes a concoction of all the possible elements of modern culture; who eats of it eats a bit of everything. To quite uncultured people, like the proverbial peasant or shepherd, it has nothing to say; neither has it anything to say to real minds, which want a critically clean food. But for the numberless people who thriftily carry on beyond intellectual starvation and not up to intellectual plenty, it means a lot. It means their daily spiritual meal. In this sense, much more than in an economic one, it may be said that fascism, wherever it is allowed to come to power, is the creed of the lower middle classes.

The completeness with which any spiritual need, degraded to emotional appetite, finds satisfaction within the frame of fascism is, one may say without irony, admirable. But this achievement is not the work of a single genius. It was not a single grammarian who from classicism developed pedantry; it is not a single fanatic who from a religion derives a superstition. Fascism is first of all a degradation of romanticism, both cultural and political. It is not a revolution, as often boasted, but an involution. This transformation was of course collectively produced. Such wide disintegration could never possibly have been the exploit of one single hero. It must be granted that the bacteria of the disease have circulated since the beginning in the blood of romanticism, a body which never enjoyed a single moment of wholly healthy consciousness.

Examples of the stupendous, although instinctive, skill with which any spiritual requirement of romantic mentality is translated into purely emotional impulses can be picked up at random. How far can fascism be Catholic or pro-Catholic, following the

path of romantic pro-Catholicism? Certainly not in so far as Catholicism includes elements of Christian ethics or any kind of supernatural belief; but the pomp and luxury of the ritual is coveted and emulated, the pyramidal symmetry and loftiness of the hierarchy and organization is admired as the grandest architecture of history. Therefore the attempt at imitation. It is beyond doubt that the model for the fascist political system was found in the Roman church. The dictator has the position of the Pontiff; every pronouncement of truth and every appointment of officials emanates from him. He is, at least in theory, secretly elective; the electoral, and somehow consulative, body is the Grand Council, an equivalent to the Consistory and Conclave. The Roman church contributed also the support of its Syllabus, a grim condemnation of criticism and reason, which did not lack courage nor, as became clear after a while, a remarkable amount of success.

Further, how far is fascism Protestant? As far as Protestantism can be interpreted, by those who like such interpretations, as the disruption of ethical codes and the foundation of any ethical imperative in the spontaneity of any individual genius, or grace, or passion: whence the self-sufficient ethics of the brigand, of the tyrant, of the pioneer, of the poet, of the hero, of the saint. How far is it democratic? As far as democracy too has its grandeur of ritual and ceremonies: crowds, well ordered mass demonstrations, plebiscites, parades. How far is it socialist? As far as socialism implies the concept of struggle (i.e. fighting, sport) and as far as the Marxist Manifesto of the Communist party denies "eternal truths such as freedom, justice, etc.," and strips away the Platonic attire in which for millennia the harsh reality of hungry interests has hidden. How far is it martially inclined? As far as war can be fought with fifes and drums and words — for down to the present, and one hopes into the future, its zeal for war does not reach for weapons more deadly. How far does it care for peace? Certainly not in connection with any education of the people to feelings of peace, which is the only way of really fostering peace, but as far as speeches in behalf of peace may attain the sheer beauty of *Real-*

politik and of Machiavellian tricks. Even in minor appearances, how far is the Roman salute Roman? Was it really the salute of the Roman citizen, or of the slave? This does not matter, especially for Germans. It is beautifully dramatic; it is proud and strong; it looks like an exercise or even, eventually, like the threat of a straight blow; in any case it implies a display of energy.

This proves indeed to be the constant substance under the flow of fascist appearances: the romantic cult of energy — or violence or passion — transferred if not into real historic deeds at least into a ritual performance. Hitler says, "We think with our blood": a motto which might well have been adopted by the primitive tragic hero, such as Lessing conceived him, or by any leading character of the Storm and Stress literature. Hence the fascist evaluation of revolution and war. There have always been revolutions in human history; but they were considered by moralists and historians as sad necessities which it would have been wise and lucky, if possible, to avoid; and the theory of revolution as the loveliest and most admirable of human social expressions is thoroughly modern. The Christian, especially the Protestant, experience of conversion and grace, which is a kind of individual revolution, gave the mightiest impulse to this conception, whose vigor increased through contributions flowing from various philosophic, scientific, political and literary sources. The lurid glamor of modern revolutions from the English to the Russian, but especially the French, added a fantastic suggestion which worked decisively on emotional complexes. Finally in the footsteps of Nietzsche and Sorel came the fascists with their idealization of revolution as such, *Revolution an sich*. Strangely enough, both fascist countries, Italy and Germany, know in their long past much more of riots and local upheavals than of real revolutions. Italian fascism was from the very beginning approximately legal and was immediately legalized; the rise of Hitlerism was legal throughout. But only to a superficial observation may it seem strange that fascism upholds things that lie outside of its history and its nature. On the contrary, it quite belongs to fascist mentality to thirst for waters that do not flow.

As for war, there have been wars enough in human history; and fascism, either Italian or German, has hitherto fought none, not even civil war. But fascism, for the first time in human history, has erected an altar to the god War. "Fascism, before everything, in what generally concerns the future and development of the human race, and leaving aside any consideration of actual politics, does not believe either in the possibility or in the utility of perpetual peace. It therefore rejects pacifism, which masks a disavowal of struggle, and a cowardice before sacrifice. Only war raises to their maximum of tension all human energies and imprints a seal of nobility on the peoples who have the virtue to face it. All the other trials are but substitutes which never make a man face the alternative of life and death. Any doctrine, consequently, which moves from the presupposed postulate of peace, is foreign to fascism; and no less foreign to the spirit of fascism, even if accepted for what utility they may have in some particular political situation, are all the international structures and leagues (*tutte le costruzioni internazionalistiche e societarie*) which, as history demonstrates, may vanish in thin air as soon as sentimental, ideal and practical elements rouse to storm the hearts of nations." So wrote Mussolini under the caption Fascism in the 14th volume of the *Encyclopedia Italiana*, in 1932; and this theory has often been proclaimed by him and his followers in other but similar words, and has been widely echoed by Hitler and Hitlerism. Peace can be accepted, must be accepted some times — alack! too many times — but as a fact of existence, an unavoidable sad necessity. The ideal condition of human life is battle.

Could one imagine a more romantic suggestion? "Venez, orages désirés." One sees the Wagnerian god Thor arousing with his hammer thunder and hail. And, since this state of mind is purely emotional and imaginative, it would be of little use to advance objections. Is it really true that human life is so miserably bereft of noble trials and dangers that war, if it did not exist, ought to be invented? And is it true that the maximum of human tension is reached only in war? Goethe, who has his share of responsibility, however mod-

erate, in the making of this mentality, wrote nevertheless the superb self-epitaph of the man who desires admittance to the Islamic paradise, a "Paradise under the shadow of swords," in spite of never having brandished a sword. "Denn ich bin ein Mensch gewesen—und das ist ein Kämpfer sein" ("Because I was a man, and that means to be a warrior"). The knight-errant or professional condottiere who rode self-determined from duel to skirmish might have boasted about the alternative of life and death; so may the volunteer, although not in every circumstance. But the democratic compulsory enlistment, which the anti-democratic fascism has not hastened to discard, has sharply changed things; and the poor devil of a soldier who has to charge against the enemy's machine gun if he does not like better the rifles of the firing squad, does not face an alternative of life and death but a choice between probable death and certain death. If, however, an alternative of life and death is an inescapable test for human nobility, why not the fire trial or simply a mortal duel as soon as any boy (or girl) comes of age? Such systems, among other advantages, would have the recommendation of economy. Certainly, it can hardly be denied that this theory of war for war's sake, of war as one of the fine arts, climbs a peak of human ingenuity. Whereas people of olden times fought, or had the illusion of fighting, for their gods or for their homes, people nowadays ought to fight because war is beautiful and supreme, the sport of sports. If such is really the fascist feeling about war, peace is safe; and their battles, as they call them, will ever be those, often salutary, which they fight no differently from communists or democrats, to drain marshes, to improve crops, to have trains running on time, to exterminate flies, or to macadamize highroads. Now and then may occur a murder or a purge, like the German Saint Bartholomew's of June 30th; but this is no war, since there is no alternative of life and death for murderers or murdered.

Whether war in human history is due to fate or to human guilt may remain an open question; but never before, in three thousand years of Western civilization, was any serious attempt made to interpret war as nice and jolly, a sword dance, and the best pastime

mankind may enjoy. To be sure, Mussolini has more than once quoted Heraclitus, "the melancholy solitary of Ephesus," according to whom "strife is at the root of all things," and Hitlerites assume that all pre-Socratic philosophers were also pre-Hitlerites. But, to say nothing of the fact that they are not usually adept in the difficult field of pre-Socratic philosophy, the fact must be taken into account that Socratic and post-Socratic, not pre-Socratic, philosophy gave the decisive imprint to ancient thought, and that the attitude toward war of pagan poetry and philosophy was scarcely different from that of the Jewish prophets and of the Christian disciples. The oldest monument of Mediterranean literature, the *Iliad*, knows certainly the emotional "joy of battle," but defines war, even in its first pages, as "the evil war" (*pólemos kakós*), and aims at forgiveness and peace. The *Aeneid* is characterized throughout by a longing for peace; and Christianity, at least theoretically, could only deepen this longing. Even the Emperor Charlemagne of the *Chanson*, though not recognizably a dastard, tears his beard when the Angel brings him the news of another war that has to be started; even in the grim *Nibelungenlied*, Etzel and all the other heroes would, after all, prefer peace, if peace were only possible. No doubt, strife is at the root of all things; but the inference that therefore the mutual killing of man by man is metaphysically necessary—indeed, that war is the richest cream of spiritual existence—is just a sophism of the meanest sort; as if on the premise that water is a necessary factor in human diet someone were to draw the conclusion that ocean water or boiling water, being supremely waters, make the best drinks for human meals.

Only in very recent times, with the "revolt of passion," has the cult of war grown up; for war is passion. Napoleon, with his startlingly visible glory, embodied the ideal far better than Schiller's imaginary robbers or the schoolmaster's excerpts from Plutarch's heroic biographies. Goethe in his *Euphorion*, half Byronic, half Storm and Stress, knew how to translate into song the scorn of pacifism that had already been formulated in plain prose, several decades earlier, by Moeser and others:

"Dream ye the peaceful day?
 Dream, then, who may!
 War! is the countersign:
 Victory, word divine."

Although the Chorus objects:

"Who peace and unity
 Scorneth, for war's array,
 With impunity
 Slays his hope of a better day."

On the crest of the same wave foamed Schopenhauer's pessimism, and, as a deduction from Schopenhauer, came Wagner's music and controversial writing. Wagner is the genius who gave flesh and blood to the most expressive of modern myths: Siegfried as a demigod of irrationalism and of adventure for adventure's sake. Wagner, too, combined German self-deification with anti-Semitism, a tendency which never before had shown the tremendous emotional swing with which Wagner was able to endow it.

Later Gobineau and others carried the tendency forward with the tale of German superiority, founded substantially on nothing but the thrilling pamphlet in which the Roman historian and orator Tacitus transferred the traditional Arcadia, begemmed with the virtues of early patrician Rome, to the German woods: a utopian republic which he contrasted with the corruption of the Roman Empire. Then came Darwinism, with the struggle for existence and the survival of the fittest; then pragmatism (and, why not, Christian Science, and, why not, theosophy, and any kind of occultism) placing imagination and will above truth and reason. Meanwhile Nietzsche—the grandest storm on the horizon of human thought, as Andler aptly said—placed the cage of the "blonde wild beast" on the meadow where Rousseau's innocent savage used to play on his reed pipe.

Is it necessary to repeat that these philosophies and arts and these intellectual heroes, major and minor, are not, each and all, directly

responsible for fascism? That a full enumeration of the elements would be interminable: that the genealogical tree of fascism is as leafy as a weeping willow? The disintegration of European thought from the decline of the eighteenth century to the dawn of the twentieth — a disintegration which did not impair, and even occasionally stimulated an astounding wealth of creative energy—took many directions; and fascism gathered from every direction whatever suited its requirements. It skimmed, one may say, anthropologically, the romantic and post-romantic mentality, quite unprejudiced in the choice of details, provided they might be arranged along the main line of fascist impulsion. This consists in a strenuous and, in spite of the multiplicity of appearances, a very coherent opposition to any form of rationalism and Platonism in the interpretation of history; and, therefore, especially an opposition to the latest concrete experiment in rational idealism: progressive democracy as it was conceived in the philosophies of the eighteenth century. Further, fascism consists in the rejection of any fixed goal or permanent aim, in the belief that change is substance, passion is virtue, force is right; or, for those who like concise definitions, fascism consists in the substitution of the idea of power for the idea of justice. Any other definition misses its proper intention; it would not touch what is specific in fascism and what is common to all brands of fascism.

As for freedom, fascism takes equitably into account—and not contradictorily at all — both extremes of the post-romantic disintegration: the super-individualistic, anarchic, solipsistic extreme, and the reactionary, obscurantist, herd-like opposite. The tyrant, or hero, is free, so far as the Superman or Stirner's *Einziger* can want to be free; hence, his rebellion against any law that might be imposed on him, League of Nations or international codes. But slaves are slaves. Chains, forged either by church or state or in the underworld of conservative ethics and complexes, are equally good; for how could He be free, had He no slaves?

All that precedes is tantamount to saying that fascism, if it were a real thing, could claim the glory of being the most deeprooted

involution or revolution in the course of our civilization, "the grandest storm that ever burst on the horizon of history"; subverting both the Christian teaching of love and the classic doctrine of permanent justice; as its ultimate achievement looming a bifront Janus, one face Antichrist, the other Antiplato. But is it a real thing? Has it outgrown the literary, musical, aesthetic cradle where it was nursed with slogans and *leitmotive*? True, there has been some castor oil, some blood, a few concentration camps, a little, perhaps not so little, suffocation. There is also a good deal of talk about the corporate state; as if a corporation or any other kind of institutional organism were even conceivable so long as His power, the omnipotence of the despot, is totally uncontrolled. But what will such historic scenery look like from the height of the future, say in a hundred years, if fascism did not go further? More chronicle than history; wavy outline, no mountain range; all in all a postwar neurosis, and an epigonic output of literary aftermath. Most of it still exists only in speech, journalism, song, cheer, advertising, broadcast. Public utterance by word of mouth and the circulation of the daily paper, this unavoidably democratic tool, is managed as a weapon against democratic thought; a paradox which, more than anything else, bares the weakness of the system. No fascist dictator has yet openly proclaimed his divine, or, at least superhuman right; no fascist dictator has retired from the profane mob behind the walls of an Escorial. A really anti-democratic belief ought to require no less than this.

Far away, almost imperceptible from the distance of the future, the tom tom of Emperor Jones fades into the jungle of nothingness.

But whatever is real in fascism, little or much, could never have come to the world, if the intermarriage of ideas, related in the foregoing pages, had been celebrated only in ideal beds, which are sterile. Not a single prophet, during more than a century of prophecies, analyzing the degradation of the romantic culture, or planning the split of the romantic atom, ever imagined anything like fascism. There was, in the lap of the future, communism and syndicalism

and what not; there was anarchism, and legitimism, and even all-papacy; war, peace, deluge, pan-Germanism, pan-Slavism, Yellow Peril, signals to the planet Mars; there was no fascism. It came as a surprise to all, and to themselves too.

One may imagine all the possible interrelations of ideas and all their thinkable results, one of which undoubtedly was fascism, although overlooked by prophets; but such results are bound to remain mere day dreams, ambivalent or plurivalent hypotheses, unless someone comes and grafts the living shoot of a real volition upon the sterile stock of the imagination. This is the final issue in history: personality. No collective explanation, either economic or dialectic, can dispense with it.

Why did not fascism arise in Russia? Because, the answer runs, the components of Russian culture were Czarist mysticism and mystic communism; there you have the resultant in communistic Czarism, or Bolshevism. Why not in the United States? Because, here also the answer is at hand, her youthful sturdy innocence preserved her from both major diseases of sophisticated Europe: the tuberculosis of eager pessimism (Schopenhauer) and the syphilis of megalomania (Nietzsche).

But why did it not arise in France, where teachers of obscurantism and hatred, from de Maistre and before to Maurras and Daudet and after, had been quite a college? The sabre rattling of General Boulanger did not impale even a mouse; Jacques Lebaudy died as emperor of Sahara; Coty, the Corsican of the twentieth century, died a short time ago as a perfumer; and the Pretenders are charming gentlemen.

England too had her share, a large one, in the disintegration of romanticism, mainly in the aesthetic and literary field, although not without encroachments on the neighboring fields of ethics and behavior. But Oscar Wilde did not set himself up as Prince of Wales; and if it must be granted that, had fascism conquered England, Irish sophistry and Popish revival would have found in fascism its good sides, nonetheless G.B. is still only G.B. and G.K. still wears no mitre.

Finally, why did not fascism appear first in Germany? We have of late heard an American sage utter the judgment that fascist mentality is un-German. This is no doubt inaccurate; no doubt a large majority of the intellectual elements of fascism had their fatherland, primitive or adoptive, in Germany. But fascism did not, however, spring up first in the furrow where Fichte or Hegel, Wagner or Treitschke, Gobineau or Chamberlain or Bernhardt or Spengler had sown; neither did corporatism, in spite of Adam Müller and Othmar Spahn. It was a long, wearisome way from the beerhall putsch to the plebiscites; and even the first putsch was started several months after the march on Rome.

Why then did fascism arise first in Italy? Because Italy had had her share, with Vico and Gioberti and others, and finally with the Pope of the Syllabus, in the shaping of neo-reactionary doctrines? This share had not been decisive, and had lacked the rhetorical spell appealing to the masses. Because Italians had not been long enough accustomed to political and intellectual freedom? This is, as already emphasized, generic for many nations, not specific for Italy. Because, more than any other nation, they had been accustomed through two thousand years of world empire and universal church, across dramatic peaks and valleys of majesty and misfortune, to loftiness of political imagination, and at the same time to the most dejected renouncement of personality in public life and to the most daring experimental versatility in political thinking? This is a better reason. They were prepared to accept anything strange and new, particularly if the novelty promised somehow to revive the hereditary complex of Roman superiority and to check the stubborn, although scarcely reasonable, complex of modern inferiority. They were also hereditarily ready to give up their personal rights that a collective imagination might thrive. But this too would have remained a theoretical reason, had the Man not come. A hundred Machiavellis cannot breed a single Prince.

The Man was not the Marquis and Professor Vilfredo Pareto, about whom we have already begun to hear much idle talk in this country. Pareto was a rather difficult nobleman, who transferred

the loathing for plebeians that saddened his genteel blood into a rather confused and pretentious system of aristocratic pessimism. Much of what is good in his work is a plagiarism or unavowed borrowing from the Italian jurist Mosca, who had already discovered that groups and elites, not undifferentiated masses, are the makers of history. Many details, especially in footnotes, are striking; and they are often the fruit of an original and rich scholarship (even if at times a bit whimsical), especially in ancient history. Much of what is bad is the inadequate and positivistic ambition to classify human history as a kind of natural science (*vide* Taine), nay, as a branch of mathematics. Nobody ever read him except in indexes, abridgments or book reviews, or in browsing. It is often reported that Mussolini, when a young wanderer in Switzerland, attended some of his classes; probably an opportunity, unusual with him, for a rest.

The man of destiny was Gabriele d'Annunzio: a great poet, so far as his greediness for life allowed him greatness in poetry, and a real man of action, so far as his poetic talent allowed him real action; a Bryon raised to the *n*th power. Now an old man, grumbling behind the walls of his freaky Escorial, the Vittoriale on the Lago di Garda, he was once a phenomenon unique in history: a poet who meant what he wrote, and lived, if not up to his full success, at least to his fancy. He had collected in one single trough all the distillations and drippings of the romantic witch-kitchen: titanism and sadism, voluptuousness and despair, Nietzsche and Verlaine, Mona Lisa and Yseult, La Belle Dame sans Merci and the Holy Virgin, the saintliness of the peasant's family, the pious silence of the cloister, the beauty of slaughter, of fire, of tyranny, of treachery, of bravery, of Rome, of sacrifice. Everything that is fascist is in his volumes, and various other things that fascism later dropped. Early in the new century he had carved the line, "*Arma la prora e salpa verso il mondo*" ("Arm the prow and sail toward the world"), which, incidentally, is rather a bewildering sailing direction. Certainly a genius, even if he had only written. But he did more than that; he acted. As war came, he went warring, an

individual warfare incomparably more striking than Byron's in Greece. He fought his own war, indeed as a potentate strictly allied to the King of Italy, but choosing whatever gallant enterprise on land, in air, on sea, suited his taste, and totally ignoring any other discipline or obligation; a self-determination unprecedented except perhaps in *Orlando Furioso* or in *Don Quixote*. Even the military rank that he adopted, *Commandante*, although apparently borrowed from the navy, was, in more or less secret intention, the literal translation of the Roman *Imperator*. As peace, or at least armistice, came he was heard saying, "I smell the stench of peace." Shortly after at the head of a handful of people, although meeting no military resistance, he seized a city, Fiume, challenging the wrath if not the guns of all the Great Powers, and there he settled, a Signore and monarch, like a condottiere of the Renaissance. There he invented or perfected everything: salutes, speeches from the balcony and choral cheers from the crowd assembled underneath, rites, processions, oaths, transvaluation of Faustism and perhaps of Mephistophelianism, into a mysticism of action. Even corporatism has roots in d'Annunzio's love of the beauty of guilds in the mediaeval Italian communes, where everybody belonged to an "art," which is, in a way, the equivalent of saying that everybody was an artist. It is an effect of this leaning far more than it is an enactment of Müller's and Spahn's highbrow speculations, a derivative from syndicalism or a loud echo of what, more modestly but more successfully, had been achieved a generation earlier in democratic Australia and New Zealand under the compulsory Arbitration Act. A year or so later some shellshots of the Italian regular forces drove him from Fiume; he withdrew, undisturbed, to his fanciful Vatican on the Lago di Garda, where a real warship with real guns lies, far away from any water, on the hills of the poet's estate, and might some day sail anew toward the world.

A failure, when compared to the promise of dreams; but a huge achievement in the difficult realm of things. If d'Annunzio, some twenty years earlier, had conquered the *jeunesse dorée* and the

naive youth through little more than his admirable poems and his smart riding on horseback, now, giving evidence that "anything is feasible" (or almost), he swept all the lower and middle emotional strata of the country. Other experiences of the same kind loomed in the memory of the race: Caesar, Columbus, Napoleon, Garibaldi in the grand style; Cola di Rienzo at about the level of d'Annunzio; the adventurers, from the Renaissance to Casanova and further, in the woodland of irresponsible pioneering. Perhaps this feeling that history is inventive, that the world of reality is plastic and obedient to a strong, creative hand, belongs to Italians more than to other nations. The deed of Fiume aroused many hearts.

Could philosophy have diked the land against the wave of mystic activism? Philosophy had enjoyed great popularity in Italy during the first two decades of the twentieth century; and the authority of Benedetto Croce, a great thinker and scholar, had not been considerably impaired by his pro-German, or neutral, attitude at the start of the war. Some tendencies of his ethical and aesthetic taste entitled him, in a way, to claim the national office of an anti-d'Annunzio. But Italian neo-idealism, either in the shape conferred on it by Croce or in the variant of Gentile — who, in fact, joined the Fascist party as early as 1924 — had, and still has, no fundamental objection to nationalism and fascism. It asserts, in the wake of Hegel, that "all that is rational is real, and all that is real is rational"; if so, is not nationalism real? Is not fascism real — so far as it is a reality? And how, possibly, can reason, or philosophy, oppose them? Besides, this philosophy is impregnated with a considerable amount of belief in the state, and in the national state as the highest possible attainment and the broadest possible community through which the individual is allowed to come in contact with the universal. It expressed also, indefatigably, a bitter dislike of Mazzinianism, democracy, freemasonry and of any kind of abstract, utopian, "eighteenth century mentality." The short autobiography which Croce composed on the eve of the Italian intervention in the war, in 1915, is very interesting in the candor with which he confesses his slowness, almost sluggishness, in political curiosity and

interest at the beginning of his career. There was an approach to socialism, followed by a quick disillusion. The only constant element in his political temperament from adolescence onward had been a feeling against the liberal and democratic "rhetoric," and an aversion to the abstract thinking of the "eighteenth century mentality." He had raised, or created from nothing, the reputation of a writer, Alfredo Oriani, now canonized among the prophets of national fascism. In his most brilliant if not most successful book, *Philosophy of the Practical*, he had inserted a short but eloquent defense of the Holy Inquisition, which was "really holy." Approximately at the same time he warmly introduced to Italian readers Georges Sorel and his "Reflexions sur la violence." This was a big event. The Italian *jeunesse dorée* and the honest fanatics — often former socialists and syndicalists of extreme vehemence — did not have to bother any more about the intellectual quality of the suggestions of violence that came from the poet d'Annunzio. Sorel's pamphlet, with Croce's preface, stamped the seal of serious learning on their passions; philosophy, so they felt, legitimized poetry. In the following decade Sorel was far more popular in Italy than in France, and he liked Italy very much: an experimental zone where, perhaps, the toilsome nail work of this misanthrope scratching nervously on the facade of contemporary civilization might help to bring about some crumbling worth the while.

In the municipal elections of 1914 at Naples, Croce headed the conservative parties, *Fascio dell' ordine*, against the leftist block. At the start of the war he was pro-German or neutral; he never agreed with the interpretation of the war as making the world safe for democracy. This war had to him no ideal meaning at all. Certainly dialectic thinking is difficult and noble, and in the very many things that Croce wrote and said about politics and history in the making there was ever a kernel of truth; but dialectic action is impossible. Hamlet may talk and sink, Fortinbras must choose. So far as Croce was a Fortinbras, directly concerned in action, he had to choose; and at the very decisive moment, which was the close of the war and the immediate morrow of war, he chose to put all the

weight of his work on the side of nationalism and pre-fascism. The eighteenth century mentality of Wilsonians and Mazzinians was necessarily hateful to him; he had already announced the death of socialism; he minimized the League of Nations; he scorned the idea of "State as justice," again and again upholding the state as force; he stressed national differences, such as those between "English and Russians, Italians and Croats, Christians and Turks"; he ultimately decided that politics cannot "be treated as ethics, whereas politics (this is the plain truth) is politics, just politics, and nothing else but politics; or, if you want me once more to repeat the tenet and comparison that are dear to me, the morality of politics consists wholly and only in being excellent politics, as the morality of poetry, whatever the incompetents may say, consists uniquely in being excellent poetry."¹ In the following years, under fascism, he has written much finer things, some of them quite beautiful; he has steadily drawn nearer to the ideas of Europe as a unity and of political freedom, though not yet giving an adequate philosophic definition of this latter idea; he certainly belongs more to the future than to the past, for a man belongs where he has most suffered and hoped. In firmness inspired by personal pride and by disinterested conviction he withstood and withstands fascist threat and fascist boycott. He has helped as no one else has to build a bridge between the generations of the intelligentsia. This is very good for the future, although it does not entirely make up for the past. During the fascist rise Croce's philosophy and attitudes did not, to be sure, contribute an impulse comparable to d'Annunzio's; but neither did they present any real obstacle. Overstating, as usual, things moderately true, fascists claim him as one of their forerunners and assume that he, not they, took the wrong turning.

Now the apple hung ripe, ready for the strong quick hand that would stretch to pluck. There was, somewhere in the huddle, the hand of Mussolini.

He had learned from Lenin and Mustapha Kemal that the coup

¹ *Pagine Sparse, Serie Seconda* (Naples 1919) p. 258 and *passim*.

d'état was possible also in contemporary states. Indeed, both these coups d'état were toward the left, in the supposed main direction of history; but d'Annunzio had taught that anything is feasible (or almost) with no matter what intellectual or emotional stuff. Mussolini was an anarchist and an artist. Endowed, no doubt, with an exceptional and exceptionally well trained ability for handling human passions, he shared also the natural inclination that such ability usually carries with it: the inclination to prefer passions easier to handle. At the close of the war he was at a crossroads. Had his intellectual background and his moral belief been rocks of steadfastness, he would have turned to the road on the left; toward socialism and Mazzinianism, toward proletarian, progressive, scientifically inspired revolution or reform; there lay all the passions and cravings of his feverishly staring youth. This choice offered chances of failure, very many of them; and some of real greatness in history. But his adventurous and mixed reading could not possibly have bestowed on him an intellectual supply better than the sophisms and *trahisons de clercs* which he relished every day, nibbling the famed books of his time; he personally went so far as to suppose that Einstein's relativity means that there is no real truth and that everything is just relative. After hesitations, the content of power grew meaningless before his need of power. On the opposite road there were nationalistic emotionalism and the fear of the owner classes; all that he had despised and hated. But they were the forces at hand, under high pressure, ready to start, while the socialist throng had proved helpless. He was an anarchist and an artist, and the temptation was too strong. He reached for the next opportunity. He got it.

Probably he is sometimes restless, and dreams of a second chance.

Hitler, fundamentally, is nobody.

He learned, in turn, from Mussolini the lesson that everything is feasible (not almost), that a reactionary coup d'état is thinkable even after the Reformation and Kant; that individual pioneering is possible even in the heart of Europe.

He merely translated, engrossing it, Mussolini's system back into the German language in which—though until then lacking impulse to action—it had been first conceived. The differences, such as the much talked of difference in attitude toward the Jews, depend on objective circumstances, not on the intentions of the leaders.

Hitler is only the shadow of Mussolini; but such a broad one that it seems doubtful if many sun rays for autonomous development are still left to Italian fascism. For the time being Mussolini, the creator, already looks like the precursor of Hitler, the imitator: a destiny allotted to many such geniuses.

In the economic field, and seen in the most favorable light, fascism, either in Italy or Germany, has faced the crisis neither better nor worse than communistic or democratic communities have. If so, what is the use of fascism? In the international field, the clashes between Mussolini and Hitler seem to indicate that it is extremely difficult for fascism to build a new international system. Should Mussolini, in the desire to evade the Hitler shadow, be driven into the path of liberal England or of democratic France, that would imply some consequences for his future in Italy; since, in the ultimate issue, foreign policy and domestic policy are interdependent.

Is the alternative war (which, as Mussolini quite recently said, with a quotation from Proudhon, "is of divine origin")? Who can wage it, or where can it suddenly explode from the patiently accumulated heap of explosive material? Or is the alternative revolution? Or slow disintegration and gradual merging in the ordinary flux of things? Such queries may be left to fortune tellers.

There are, beyond doubt, positive and creative elements in fascism. First, the appeal to energy (although energy must know its aim, and the aim must be a good one). Second, the appeal to social order and discipline (although the basis of this order must be shifted, and the aim must be collaboration among freely ordered nations, not war, which is the worst of disorders). Third, the criticism of democracy and parliamentarianism in their decay (although a better democracy, not despotism, must be the inference).

Fourth, and best of all. Italy and Germany came last, not yet two thirds of a century ago, into the row of modern national states. They were immature. Fascism is giving them the inner experience of struggle and character that France and England had in the late Middle Ages, and America in the Civil War. Much of Germany is still a storage place for the pious safekeeping of mediaeval memories; Italy is still a peninsula jutting from the ancient world into the new. Involuntarily, but at highest speed, fascism is burning in both countries all the material of the past: personal and dogmatic authority, monarchy and church, classic and romantic pedantry, daydreaming and involuted introversion. From fascism both nations will emerge, soon or late, renovated, quite European and modern, and makers of Europe.

For the rest, the conclusive words are in Milton's *Paradise Lost*, XII, 95 ff.

Tyranny must be,
Though to the Tyrant thereby no excuse.
Yet sometimes nations will decline so low
From virtue, which is reason, that no wrong,
But Justice, and some fatal curse annex'd,
Deprives them of their outward liberty,
Their inward lost. . . .

It has also been said, "Deeds, not words." But it must be said, "Words, not deeds."

It was first sinned in the Mind. In the beginning was the Word. Mind and Word must make it up. The intellectuals of the new time, philosophers and poets, must reject sophistry and lies; they must think in terms of righteousness and truth, and of united Europe, which is the next stage in the development toward unity of human effort. They must not feel ashamed of feeling like prophets; and they must cultivate the endurance and selflessness of prophets. They do not need to see a better world if they, "immovably centred," keep working toward it.

PLANNING AND THE MARKET SYSTEM

BY EDUARD HEIMANN

I

A SYSTEM of central planning is the opposite of a spontaneously operating decentralized market. It might seem that a clean and logical solution of the problem of economic organization would therefore demand either a return to plain capitalism or a new integrated system, call it communism if one will. An intermediate position does not appeal to the imagination. A mixture of systems is suspected of inconsistency and appears traceable to a lack of resolution. There are distinct and conspicuous advantages in either system but they do not appear compatible. Anyone who recommends an intermediate position has therefore to explain how he plans to build up a functioning system out of materials taken from the two opposing systems. The elements of the two systems must be made to interlock, and this requires us to distinguish their respective functions and combine them in a consistent and workable whole.

The scheme of economic institutions which I propose to discuss is the following. I assume separate independently managed units of production on the one hand and a centralized management of credit and investment on the other. The independent enterprises are connected through the market with other enterprises and with the factors of production and the consumers. They are also connected through the market with the central control of investment. They may either compete with one another or monopolize their respective fields. The centralized management of investments may be conceived of as a form of monopoly using, however, specific methods, whose operation we have to discuss. Among the instruments it would employ is the right to investigate the condition of technical

equipment in all plants, whether publicly owned or not. The whole system is designed to provide for stability of economic life, to prevent the wild fluctuations of the present system.

No further assumptions are required for our purpose. Particularly, we do not need to make any assumptions as to the social and property organization. It is true that the conception of a market seems to presuppose private ownership and that centralized management appears to be linked to common property. These associations of concepts are, however, far from being logically necessary. On the one hand common property in all plants does not preclude an organization of production in separate units whose managers would be morally and financially interested in their individual success, even though all profits should belong to the community as the owner. Such a market would evidently not be a capitalistic market. On the other hand the unitary will which is crucial to centralized planning may be derived from unitary property of the communist type but it may equally be conceived of as some kind of individual dictatorship rigorously opposed to socialism, or it may originate in the consent of an enlightened business community seeking to defend its long run interest in stability and security. These various possibilities naturally involve the widest divergences in the method and proportions of the distribution of incomes because of the close relationship of incomes to the stratification of property. While a redistribution of incomes is compatible with planned economy, the planned economy does not necessarily involve such redistribution.

Of course I do not deny that planning and the centralized management which it involves bear on the questions of property and income and on the social organization as a whole. This needs to be emphasized because there is in this country an astonishing disposition to treat the problems of planning as if they were of a purely technical character and had no essential bearing on the social structure. Whether a given social structure can apply a given plan of reconstruction is not only a technical but also a political and spiritual question. More specifically, the question is whether this so-

ciety can provide the organizational and moral prerequisites of reconstruction without giving up its essential structure and underlying values.

II

We should need no planned economy if the spontaneous activities of decentralized management produced the universal harmony predicated by the earlier classical writers.¹ These writers assumed that the free fluctuations of prices express the fluctuations of demand and bring about a corresponding movement of supply, thus adjusting supply to demand. The first part of this statement, as we shall indicate, is true and offers the indispensable basis for any genuine accountancy system. The second part cannot be maintained and should be replaced by a more realistic theory. It is necessary to distinguish between the two functions of the price system, first accountancy and survey of economic fluctuations, and second active control and regulation of production. Since the reputed mechanism of automatic self-regulation does not work, deliberate regulation is necessary; but it is in terms of free prices that we must measure the response of demand to such regulation.

The classical theory of the harmonious response of supply to a given change in demand assumes a closed and static system of economy within which a change in demand in one particular market is necessarily compensated by an equivalent change in the opposite direction in some other particular market. Under these conditions the prices of the commodities concerned would move in opposite directions and would stimulate a corresponding shift of means of production, so far as technological rigidities permitted.

This theory, however, does not apply to an open and dynamic system. In a static system a fall in wages in a given industry or area would expel labor and so tend to restore the original level; but in a dynamic system it is possible that the effect of a fall in wages would draw into employment other members of the worker's family in order to maintain the family income, thus forcing a further

¹ Not by Ricardo.

fall in wages. A fall in business profits may stimulate entrepreneurs' activities in order to meet the requirements of a fixed debt; an appreciation of money which in a static system would result in an increase in the production of gold and a consequent correction of the appreciation is likely in a dynamic system to produce a depression with a shrinkage of credit which would increase appreciation far more effectively than any possible increase in gold could reduce it.

It is particularly in connection with capital equipment that the dynamic situation proves recalcitrant to static theory. If the available labor supply increases either because new strata of the population are drawn into employment or because workers are displaced by mechanization, new jobs are imperatively required, but this additional supply of jobs is far from being automatically provided by the free play of competitive forces. The wages which the employer saves by mechanizing existing jobs and dismissing the workers might indeed be used as wages for additional jobs only in case the capital equipment for these additional jobs were also supplied. Although the effect of an absolute or relative increase in the supply of labor would be to reduce wages and thus to increase profits and the possibility of saving out of these profits, any new capital thus created would appear too late for equipping the additional jobs, nor have we any reason to assume that even the final accumulation would be adequate to the purpose.

All these and many other conceivable failures of the market in the automatic adjustment of supply to demand constitute the case for comprehensive and deliberate planning. The core of a scheme of planning is obviously the regulation of credits and investments, as this would necessarily involve an indirect control of profits and wages. In a later section we shall examine some of the details of the control of investments.

Planning thus conceived would, however, not make impossible the adequate expression of the new situation in terms of prices. Under a planned system the supplies of the several goods would be different from those which would have been the outcome of

an automatic play of the market but would have to prove appropriate to the situation of demand through realizing adequate prices. If the price fixed at the outset does not secure an adequate reaction of supply to changes of demand it still remains true that the response of demand to changes in supply would be adequate. What determines the price of a given supply is the purchasing power of consumers available for its purchase. The price system serves satisfactorily as an indication of the adequacy of production, even though it fails as an active regulator of production.

A survey of the demand for goods for ultimate consumption is relatively easy, and would be much simplified in a socially more uniform system with a corresponding standardization of consumption at least for the great majority of goods. An excess or deficit of production becomes directly visible, if not through its influence on prices, through the failure of customers to clear off the stocks or through an unsatisfied excess of demand. The real importance of the system of planning lies within the sphere of production, where it dictates the necessary adjustments throughout the series of production processes necessary to meet a given situation of ultimate demand. This is achieved by translating the price system into an accountancy system.

The books of any one firm afford a survey of the whole economy in so far as it is relevant to this particular business. Nothing but prices are entered in these books, the prices received for sales and paid out in purchases. The function of bookkeeping is the current comparison of cost and return. The prices received express the relative purchasing power of buyers for the particular good, or to go a step further back, for the special application of labor and materials to the production of that good. On the other side of the account the bookkeeper enters the prices paid for labor and materials in competition with other possible applications of labor and materials. It is the entirety of possible uses which determines the general price of labor and materials; it is the utility to the consumer of the particular use which is expressed in the price of the product. The significance of bookkeeping then consists in putting any ap-

monopolies also interfere this way

plication of labor and materials to the test of comparison with all other uses possible at the same moment.

Assuming a given demand for a particular good, or ultimately for a particular combination of labor and material, any change in this demand would, through the working of the accountancy system, affect the situation of all businesses which have to deal with the same category of labor or the same materials. There would be more or less of that labor or material available for other purposes when less or more of them respectively is devoted to that specific combination. These shifts in demand would find expression in the automatic shifting of the prices of labor and materials. Every unit of production can immediately learn from the relative weight of these prices in its actual account what readjustments it must make. Such instantaneous reflection of any change throughout the whole system evidently presupposes free markets not only in the sphere of consumers' goods but equally in the sphere of producers' goods, including the factors of production.

In the foregoing it is assumed that the impetus to change originates on the side of demand. Assuming that the impetus to change comes from the side of supply, the effect on the accounts of all those concerned is not different. Such a change in supply might originate in a technological change which replaces the quantity a of the material x by the quantity b of the material y and therefore it may be accompanied by an upward movement of the price of y and a downward movement of the price of x which would affect in varying degrees the accounts of all those businesses which have to deal with x or y or both.¹ Changes in the market situation are ob-

¹ A central board, in order to ascertain what prices of the materials would be in harmony with the technical requirements and the volume of demand, might send questionnaires to all factories concerned and ask them how much of the one and the other material they would buy if the prices were set at m and n respectively and how much if the prices were m_1 and n_1 or m_2 and n_2 and so on. Thus the board might find out the correct prices, i.e. those which would cause the producers to clear off the existing supplies of the materials. Under this assumption a staff of statisticians and accountants would finally arrive at the result which a market would yield automatically, and without diverting one man from directly productive work. If all the mathematical permutations and combinations of prices for the materials concerned were submitted to the producers the adequate combinations would be

viously much more far reaching when derived from technological changes of a possibly revolutionary character. The wider the ramifications of production the less possible would it be to make an immediate survey of all repercussions and the greater would be the need of depending on automatic and instantaneous adjustment through prices and accountancy.

It is usually assumed that monopoly represents an exception to the free price system. Monopoly is of course a deliberate intervention in the market, and it artificially increases the relative scarcity of supply in the presence of a given intensity of demand. Thus it interferes with the regulating active function of the price system. But monopoly does not abrogate the passive index function of price, which indicates the situation and requirement of demand. An illegitimate cut of supply contrary to the suggestion of prices is adequately expressed though not cured by the higher price brought about by that cut. It is a merit of the free play of prices to reveal the exact degree of disharmony produced by private monopoly.

The free price which we are studying is therefore not limited to the more or less fictitious competitive market but applies to any situation where buyers are formally free in their response to the policy of suppliers. Therefore the whole realm of monopoly is a realm of free prices in our sense. This is true even though both supply and price are fixed by suppliers; for it remains to be seen whether buyers will accept the price for the given supply and thus confirm the correctness of the suppliers' decision or will force a change of the market by putting to the seller the alternative of either reducing the price or renouncing the sale of part of the supply.

clearly discernible. A fuller discussion in favor of this idea may be found in the instructive paper by Kurt Mandelbaum and Gerhard Mayer "Planwirtschaft" in *Zeitschrift für Sozialforschung*, vol. iii (1934) p. 228 ff. But this logical possibility is a technical impossibility. Economic problems are not solved or eliminated by expressing them in strictly logical terms. Logically the adjustment of supply to demand is simple, but to make this adjustment through actual working institutions is another matter.

The theory of monopoly, as elaborated through decades of economic study, recognizes that even private monopoly need not necessarily pursue an oppressive price policy. Monopoly may involve the organization of a whole industry under unitary direction and may thereby reduce costs of production to a level below that of most competitive producers. Private monopolies are often able to lower their prices below the price level that had been established by competition, although they may make higher profits than the competitive producers had enjoyed. A public monopoly, whether in a socialized or in a private business system, might assign the whole gain in productivity to the buyers by enlarging its production so as to make the price equal to the new cost. Private monopoly invented, and public monopoly may use on behalf of social ends, the method of differentiating the price according to the purchasing power of the various classes of customers. By charging less than the cost to the poorest class and covering the loss at the expense of the richer classes, monopoly may contribute toward approximating real incomes to each other. This principle may be applied to various qualities of the product or even to different products of a public corporation or of a partly or entirely socialized system. What is then needed is to expand the production of the cheap product so as to satisfy the demand artificially aroused by the artificial reduction of the price below the cost; the sales of dearer products will diminish and production forces will have to be transferred from the diminishing section of the industry to the expanding section. If the monopolistic gain is treated theoretically as a tax we finally approach the system of gratis deliveries covered by taxes as in schools, hospitals and parks today.

It need not be emphasized that all this is possible only within limits, that a complete equality of real incomes in spite of differences of nominal incomes would destroy the productive stimulus and effect of these differences, and that the technical advantages of monopoly are often outweighed by the psychological advantages of competition. In its proper place, however, the monopolistic instrument is very powerful. It is also the form that must be assumed

by any control over credit and investment. Regulating investment means of course curbing it at one point and pushing it ahead at other points, something that requires a unitary survey and will of monopolistic character.

All these monopolistic instruments, much as they change and shape the market, share in the general features of the market and move within its limits. By artificially changing one of the factors of the market we do not prevent the spontaneous and correct reaction of the other factor and the exact expression of the new situation in the resulting price.

III

The difficulties of an unregulated market center in the investment sphere. Both the enormous costs and the technological rigidities of modern plants aggravate the danger, under the stimulus of gain, of irreparable competitive overinvestment in important fields. These plants suffer moreover from the inevitable ups and downs of demand, as has been shown by Robertson and with classic thoroughness by J. M. Clark.¹ What we are most interested in here is so-called technological unemployment, the displacement of men by machines.

An invention which replaces the workman by a machine may be taken as representing the typical form of technical progress in connection with the unemployment problem. So important an invention as the automobile seems indeed to involve a decentralization of transportation and an increase of labor in the transportation system as a whole. This may appear to run counter to the rule that technical progress displaces labor. But the aggregate volume of transportation has considerably increased with the extension of the use of the automobile and this will account for part of the increase in employment in the transportation industries. Disregarding the labor that is in part pleasure driving, the wide use of buses and trucks represents a new economic service for the most part. We shall

¹ Robertson, D. H., *Banking Policy and the Price Level* (London 1926) and Clark, John Maurice, *Strategic Factors in Business Cycles* (New York 1934).

later see the progress of displacement when the less efficient vehicle gives way to the more efficient.

It is true that the total volume of industrial occupation has grown instead of diminished as a result of technical development. We have to distinguish the two tendencies of mechanizing an existing job and of creating additional jobs on a given level of technique. The first means a decrease, the second an increase in the demand for labor, and an equilibrium of the two tendencies is required. This equilibrium, however, is not automatically attained. Under the favorable conditions of the prewar period, a permanent increase in the volume of industrial and commercial employment took place in spite of periodic interruptions and fitful unemployment which was gradually reabsorbed. As indicated above much capital is required for equipping a job and in spite of the current stream of capital formation, a fitful mechanization which automatically sets the wages of the dismissed workers free for other jobs does not automatically find the additional capital equipment for these future jobs. It takes time to bridge the gap, particularly when the mechanization movement is active and general.¹

The rate of interest fails as a regulator of investment. It does not even control the current supply of savings. As an instrument for the control of the progress of technological change it is ineffective or rather perversely effective. The rhythm of technological progress involves first, the ordering and building of additional machines and second, the squeezing out of the workers through the use of these machines. With the completion of mechanization of consumption industries there is a cessation in capital goods production. While the contraction of employment through mechanization is

¹ This is a brief introduction to an important German contribution to the theory of the cycle. It was derived from Ricardo's chapter on machinery in the last issue of his *Principles* and it was started by Adolf Löwe's article, "Wie ist Konjunkturtheorie überhaupt möglich?" in *Weltwirtschaftliches Archiv*, vol. xxiv (1926). The further main documents are Hirsch, Marie, *Zur Theorie des Konjunkturzyklus* (Tübingen 1929), Lederer, Emil, *Technischer Fortschritt und Arbeitslosigkeit* (Tübingen 1931), and Mitnitzky, Mark, in *Weltwirtschaftliches Archiv*, vol. xxxiv (1931). The most thorough and complete elaboration of the argument, as complete as possible without reference to the monetary phenomena, is now to be found in *Die Theorie der Arbeiterfreisetzung durch die Maschine* by Alfred Kähler (Leipsic 1933).

actualized only in the second phase of the rhythm, it becomes inevitable from the beginning of the first phase through the ordering and producing of the machines destined to displace labor. They are ordered on the basis of a given rate of interest which expresses a given supply of capital; but their own immediate effect, the displacement of labor for which new jobs and new equipment must be found, necessitates an additional capital investment for which the supply is not forthcoming except by some fortunate and unforeseen coincidence. The rate of interest affects the short run considerations which start the movement; but the long run effects on the labor situation are beyond its control. Indeed the situation is complicated further by the fact that the same amount of capital with the same immediate bearing on interest may be used either to reduce employment by mechanizing existing jobs or may open up additional employment by founding additional jobs. The two events of opposite significance for the development of the economy are covered by the same expression in terms of short run considerations. The question of whether a future need of capital equipment for additional jobs is implied in the present capital demand for building a machine is by no means answered by reference to the present interest rate. Yet this capital requirement may be expressed in fairly exact figures when we know how many workers are going to be displaced by the machine which we are building.

Hence the task of farsighted regulation of investment is clear. It must take into account the effects on the future situation of labor and capital of assigning a part of the present capital fund. A capital assignment may be possible from the standpoint of the present capital supply; and its investment may promise a sufficient return to cover the interest. These tests alone would be inadequate for the regulation of investment with a view to the future requirements which arise from a present investment of the mechanizing type. It is these potential future requirements which are crucial for the correct decision as to granting an application for capital. In case of a project for mechanization one would have to inquire at what future date the building period would be finished and the mech-

anizing and work-diminishing effect of the new method would be felt and how many workers would be affected. It is essential to note how simple and definite this problem is as compared with the usual conception that planning requires a superhuman wisdom. Unless an expansion of production and maintenance of employment on a given level is being prepared for that critical moment and capital for the additional investment is available the request for capital should be refused. Roughly speaking the long run investments which are being started during any given period should be distributed equally between the two types which respectively diminish and increase the demand for labor. It need not be necessary to say that the compensating investments in additional jobs will seldom occur in the same industry which demands capital for mechanization of existing jobs, but in other fields.

In applying the general rule, allowance must be made for the different lengths of building periods in different investments. It is also easy to modify the rule in a period in which there is a shift in the age composition of the population and an increase or decline in the proportion of the employable. This again is not a matter of guesswork but of calculation, to a very large extent at least. A by-product which may be practically equal in importance to the express aim of the arrangement is the regulation of investment with a view to avoiding competitive overinvestment in special fields. This simpler case is included in the more complicated one. As to the difficulties connected with durable goods both for production and consumption we refer to J. M. Clark's book, cited above. It is, however, clear that here too what is necessary is to curb fitful expansions adapted to fitful accumulations of demand and to smooth the trends of both demand and output. It may be added that by curbing the exaggerations of investment the rhythm of demand will be made more even inasmuch as purchasing power arises from employment in building those investments.

All this, however, though it adds new tests to the tests of the free market, is not in contradiction to it. The investigation into the economic significance of a proposed investment complements the

examination in terms of price calculation. Effective demand for the final product sufficient to cover the cost of the investment is in our analysis an indispensable condition although it is not the only one. And this condition can be taken care of by the petitioner for credit, not by the central authority whose debtor he will be. The business aspect of the question is dealt with in the usual decentralized way and is to be modified only by the introduction of provisions bearing upon the future, which the business calculation claimed to include but failed to do so. The primary initiative lies with the debtor, the regulation is in the hands of the creditor. This regulation is mainly negative; its function is to prevent investments which would be granted by a pure business system interested only in the prospective money return of the one investment but whose future effects would be injurious. The central board does not need to insert positive projects of its own into the range of projects submitted for its approval. This limitation again shows how practicable and non-utopian the working of the central board would be. In all these respects planning as described appears to curb expansion and progress. It would indeed temporarily moderate the speed of expansion in order to prevent the otherwise inevitable setback. This offers an answer to the possible objection, from the capitalistic standpoint, to a planning system designed to slacken progress and expansion. They would indeed be slackened as compared to their speed during the boom phase of the present system, but not necessarily as compared to the average speed of an entire cycle. And even if a deficit in speed remained it might be justified as the price to be paid for the gain in security of economic existence and in stability of the social system.

There are corresponding objections from the communist side. Because of the differences in the stages of economic evolution, the problem of planning is not the same in the industrialized nations as it is in Russia. From the point of view of communist planning, this difference involves an advantage to Russia, not only in degree but in principle. Grave mistakes in planning are virtually impossible in a country which lacks everything. A country like Russia

may be careless in regard to the economic calculation; it may destroy the apparatus of exact calculation which is afforded only by free prices and replace it by evaluations through decree which are of an arbitrary character even though they try to approximate free prices. Such a country may hasten progress without fear of a consequent collapse; it may triumphantly point to a speed of development many times superior to that of the older countries; it may boast that it has escaped the unemployment which strikes countries which are proceeding toward planning at a slower and deliberately moderate pace. This is not a contrast between communism and capitalism, but between the undeveloped stage of Russia as against the highly developed stage of the older countries. When one investment has been completed the planning board need not be at a loss for other investments, since any investment will become useful sooner or later. A Russian planning board may violate the equality of marginal utilities for the time being but it will be overtaken eventually. The worst danger is a wrong sequence in initiating the various plants.

The task of planning in a developed country is much more delicate and the danger of a mistake is of much greater consequence, because a wrong investment may be lost forever. Overproduction in the usual sense of producing things in excess of demand and of real wants is not to be found in Russia, but in the older countries. These countries cannot so easily start a new investment in order to reabsorb the workers who are displaced by preceding investments. These countries have to watch over the interlocking of investments and wants respectively, and they have therefore carefully to calculate and to distribute the investments to preserve the equilibrium in the labor market. That is why they need a bookkeeping with true evaluations and also a regulation of technical improvements, as Russia will need these finer instruments when she attains a similar level. It is only fair to add that the older countries enjoy a great advantage over Russia in their higher standard of living. They are not, as Russia is, menaced by starvation in case of investments that are mistaken, or that contemplate too remote a future. Russia com-

pensates this disadvantage through a combination of three factors: the tremendous power of its government to impose hardships on the people, the customary frugality and poverty of this people and finally their political enthusiasm. It follows that Russia cannot serve as a prototype of planning for the Western world. She will sooner or later have to follow the model of planning set up in the Western world.

This model turns out to be more cautious and more modest than its rival. The caution is crucial to its success, the reserve and restraint from more ambitious and far reaching policies is not. What we have described is the minimum policy which aims at mitigating and avoiding the wild fluctuations of a spontaneously acting dynamic system. Its function is mainly negative; it consists in curbing the pace of dynamic movement in accordance with the available means of maintaining the volume of employment. The amount of these means was assumed to be fixed and the task was therefore defined as distributing them in even proportion. It is, however, obvious that the formal equilibrium can equally be secured by procuring a larger supply of means—the Russian expedient in any blind alley—although, as pointed out above, there is not a similar abundance of possible investments in the other countries. Taxation or inflation might provide the means, investments of the public works type might be financed in this way. Moreover what applies to finance in private economy might also apply to it in a planning system, namely that the financial authorities would assume a good deal of positive initiative and responsibility by virtue of their wide survey and thorough information although they might also content themselves with furnishing such information to persons engaged in the actual work of production. Any shift of weight from the decentralized to the centralized sphere may increase technical efficiency on one hand, and bureaucratic rigidity on the other. The theoretical discussion has to note these two sides of the problem, but it is perfectly aware of their differing relative importance in different fields. A general theoretic discussion can contribute nothing to the most important tasks of actual organization; its function

is to analyze the working of the minimum organization at the center of a planning economy.

IV

In order that this minimum organization may be able to operate certain specific requirements are indispensable. The functioning of the regulating mechanism depends wholly on its absolute control over all investments of considerable significance, on its power to refuse a grant of capital funds if need be and thereby to prevent an investment of which it does not approve. There must be no hole in the net. Such a hole might easily be torn by the accumulation of corporation profits, the so-called self-financing of corporations. It might be torn by an alliance of the corporations and the bankers, since both are eager to secure profits and interest which a refusal of the central board would exclude.

It would of course be mythology instead of rational analysis to dispute the possibility of conflict under conditions of a strictly centralized management of state property. If the technical units of production are administered by officers responsible for this success any refusal by the central board of investment funds would destroy hope of these officers for a conspicuous achievement and a pecuniary or moral reward. Admitting this, however, the conflict is distinctly less keen when both the central board and the industry are owned by the state. In this case it would be only the manager whose interest would be harmed by a negative credit decision. Again if organized groups of workers were financially interested along with the managers in the success of the enterprise, as might be the case under some future democratic principles of organizing production, the conflict might easily become serious. Under certain conditions it would be easier to decline a request presented by a private group.

If it is assumed that property, in the main, is left in private hands, the problem is one of finding means by which the central board may impose its will upon a more or less reluctant financial world and may secure exact information concerning the financial positions of corporations seeking investment grants and the probable

effects of such grants. The records of discount and open market operations by existing central banks are discouraging as the banks did not succeed in establishing control even in a limited realm. One reason for this failure, however, is that the underlying theory was incomplete and unsatisfactory. In some respects the more general control here contemplated would find its task simpler. The survey of private and possibly injurious investments is for technical reasons possible. Profits may be concealed, modern machines and plants cannot be. A control which analyzes the technological situation is less easily misled than one which depends on financial accounting alone.

However important the technical administrative side of the problem is, the moral side is even more important. The whole system would be paralyzed from the start unless it would enlist a reasonable degree of sincere cooperation on the part of the business community itself. To impose strict control over investment upon a stubborn opposition by means of financial and administrative coercion alone would certainly not succeed. It would be necessary to work out some agreement between the central body and business as to the aims and main lines of the restrictive policy. This is not a question of ethics but of an enlightened self-interest which would take into account not only the possible loss of profit due to the restriction imposed, but also the benefits to be derived from such a scheme of organization as would preclude a breakdown which might annihilate all previous profits. Speaking in more general terms, unregulated private capitalism is doomed by its effects. From the point of view of capitalism itself there is no escape from the necessity of making fundamental concessions sufficient to avert an overthrow.

Rigid as the principles of a planned system must be, they nevertheless leave a large realm to uncentralized activities. It is not necessary that control should be all-inclusive. From the economic standpoint there is no necessity of subjecting to central control those branches of production which can become dynamic, if at all, only through their connection with the essentially dynamic

branches. Investment of a modern technological character cannot remain invisible; still less can investments in such decentralized fields as agriculture be withdrawn from the oversight and indirect control of the central body. Even the textile industry is sufficiently decentralized to be adequately controlled through credit regulation. This point is significant. It is precisely in the decentralized, non-dynamic industries where planning would encounter the greatest administrative difficulties. Indeed, if planning required a rigid centralization of management throughout all fields of production it would not be likely ever to pass beyond the utopian stage, even though it were generally recognized that planning is essential to the continued existence of a highly industrialized society. Any general centralization and socialization would be frustrated by the deadly hostility of the lower middle class of independent producers, who hold the key position politically in most countries.¹ With planning confined to the control of the present sphere of big business, decentralized industry has nothing to fear from it. The managers of the great enterprises have been trained to see the benefits of rationalization and may be won over to self-restriction and cooperation under a unitary system of control, or they may be replaced by the proletarians who are trained under the same conditions of rationalization. The independent producers are non-dynamic and traditional in their typical attitude and it would be impossible to win them over to a system involving a complete break with this established scheme of existence. As we have seen, a planned system would retain the institution of a free market where the play of prices would provide a check upon the operations of control. This market would sufficiently control the independent producers and would integrate their operations with those of the industries definitely subjected to planned control.

It becomes obvious that the market is not a sociological principle, as Marxism thought, but an instrument to be handled by various types of society with a view to various ends. These ends must in-

¹ This article is an economic complement to my sociological study, "Socialism and Democracy," in the preceding issue of *Social Research* (August 1934).

evitably shape the character of all those who operate within the market. The deliberate activities of a disciplined industrial society will therefore influence and educate even those groups which are traditionally most remote from its principles. Much as a social structure may be diversified it is one nevertheless and its underlying principles are expressed in one way or another throughout its diverse groups. The peasant in mediaeval society differs from the peasant under private capitalism and from the peasant in a post-capitalistic planned society whether equalitarian and democratic or not. The principles of a planned society become acceptable to the peasants in the measure of the benefits the peasants enjoy in their natural striving toward a steady progress. Some planned organizations of a cooperative character have been developed under capitalism even in the highly individualistic realm of farming, and more organizations of the kind would certainly come into existence if society turned to planning. These would bridge the apparent gap between the centralized and the decentralized spheres.

There is no need of a violent and forcible coordination into a planned society of the traditional individualistic groups. No revolutionary break in their existence is required in order to start and operate the system of planning. A wise policy aimed at effecting planning would offer these groups a solemn guaranty that nothing would be done in their sphere without their consent. This does not mean merely a negative attitude of toleration but a positive attitude of approval. Man is changeable and therefore invites the experiment of pressure; to what extent he should be deliberately and forcibly changed is a point on which opinions differ widely, even if it be granted that the changes are inherently desirable. The planner who seeks to force men into a mold suitable for his purposes must regard himself as the ideal representative of mankind. Planning as a practical system requires no such regimentation. Nor indeed is it merely political expediency which warns against excessive uniformity. The system will be the more inclusive and stable the less uniform and narrow it is, the more it offers special opportunities to the different types of living men.

THE EFFECT OF COMPETITION ON PRICE CHANGES IN A DYNAMIC SYSTEM

BY WALTHER LEDERER

IT is often taken for granted, without further consideration, that free competition is the only reliable means by which a deranged equilibrium can be reestablished in the economic system. Furthermore, it is maintained that free competition is the surest guaranty for the most rapid and favorable development of productivity and is therefore most conducive to a rise in the standard of living.

The latter theory is the axiom upon which the economic science of the period of growing capitalism was based and it constitutes the foundation for the belief (since no definite proof was given) that capitalism is more fitted to serve mankind than was the older regimented guild system.

The former theory that a new equilibrium can be established by competition, which developed in a much later period, had a defensive character and certainly made less pretentious claims. From the point of view of this theory it is not so much a question of rapid economic expansion as a question of a stable economy, exhibiting in the ideal case a continuous and gradual progress. In these circumstances it is assumed that free competition corrects the greatest defect of capitalism itself, namely, the crisis. Depressions, it is frequently maintained, attain to the degree of severity with which we are familiar only because free competition has been to some extent displaced. Here, too, the theory is an axiom and "principle" of economics, not a verified induction from the facts.

Our study will show that free competition by no means always attains the results attributed to it by its champions. We shall discover that it is not free competition, but rather the "obstacles" to

a free market which prevent extreme fluctuations in production and prices. It appears from our study that free competition can achieve its goal only when new industries are developing under it. This may explain why the leading business classes and the economic science of the growing capitalist order accepted this theory as an axiom; it may also explain why almost everywhere today except among traditionalists the theory encounters doubt and disbelief. It is not our purpose here to consider economic processes empirically and from that point of view to work out conclusions as to the nature of competition. Any such approach would involve a complicated work of analysis in order to isolate the effects of competition in the complex of actual economic processes. We shall rather attempt to analyze the course of the competitive struggle itself by the use of an abstract and simplified model of economic life.

As a first condition we assume that the quantity of money and credit remains constant. It is indeed conceivable that the volume of credit would change as a consequence of competition in the production of goods. In what direction the volume of credit would tend to change will be discussed at the end of this article. A study of the question, whether through changes in the volume of credit the fluctuation of production and prices caused by competition can be restricted or even prevented, must be reserved for later investigations.

We assume the following simplified situation in order to obtain a more exact insight into the working of the competitive system: An industry consists of a large number of enterprises. The number is so great that the single entrepreneur does not know the quantity of production or the costs in other firms. He is not informed about the organization of new enterprises with improved methods of production, nor can he survey the means of production held in reserve, which in case of rising prices could be put into motion. The entrepreneur is familiar only with the momentary market price which can be obtained for his product; if the price is higher than the costs of production, he will produce; if the price falls

below the costs, production has to cease.¹ It makes no difference whether a whole enterprise is shut down or only an especially unprofitable section within the plant. As a matter of principle, however, it must be assumed that plants or divisions within a plant whose costs of production lie below the price limit are completely occupied; that is, in such plants there are no unused capacities of production. Whereas in a static economic system (for instance in Schumpeter's sense of the term) differences in the technique of production of industrial enterprises by definition cannot be admitted, while in a dynamic system we are permitted to proceed on the assumption that all plants have a different efficiency. We follow here the same scheme as was employed in Thünen's analysis of agriculture by zones. The marginal producer, who works without profits, is determined by the price of the product. The difference in costs of production of the marginal plants and of the other plants is the profits. This definition of profits as quasi-rent is also employed by Schumpeter in his book, *Theorie der wirtschaftlichen Entwicklung*.

In arranging these conditions we have the intention of constructing a situation in which free competition could work without restraint. Such a situation has never existed in this pure form; there have always been hindrances and friction which have prevented this mechanism from becoming fully effective. Nevertheless we are forced to employ this scheme if we wish to deal with the problem of free competition. We shall now consider how free competition works under these ideally abstract conditions when a new plant, with more efficient methods of production, deranges the existing equilibrium. There is therefore only a single technical improvement, involving an increase in the output. In order to

¹ It is perhaps nearer to reality to say the production has to stop only when the losses through a continuation of production are larger than the losses incurred by closing the plant. Often the cessation of production occurs only when the income from sales no longer covers the costs of raw materials and wages. Therefore in order to be accurate we should have to assume that only these items constitute the costs, whereas other items usually treated as costs, especially interest and a greater or less part of depreciation, belong to net income in our scheme. The constitution of this scheme and the conclusions to be derived from it remain, however, undisturbed.

avoid complicating our study too greatly we leave temporarily out of consideration the rising prices of raw material and labor time, resulting from the greater demand, by assuming that workers are available and that raw materials can be produced in a short time and in sufficient quantities. Likewise we do not take into account the possibility that through changes in the volume of production the amount of money or its velocity might be affected. We can assume that the necessary increase in the working capital is raised through short term savings so that the amount of money remains the same, and prices are not changed. We construct a graph for this industry by laying out on the horizontal axis the physical output of production of all enterprises; on the vertical axis we indicate the prices. The area of the graph represents therefore the total sales of the industry. The plants themselves are ranked according to their costs of production. The resulting line of costs is a straight line which, to begin with, touches the selling price of the product at its highest point. This represents the situation of the marginal plant. The space below the line of costs shows the costs of production for the whole industry; the space above this line denotes the net income.

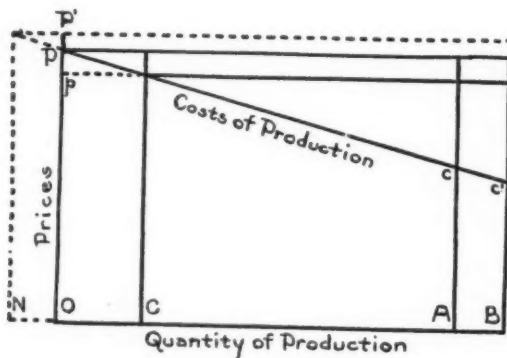


FIGURE 1

In the initial stage we have the price, P , the quantity of production, OA , and the operating costs of the most advanced plant, Ac . The newly appearing plant with the cost of production between

Ac and Bc' increases the quantity up to OB. The larger amount of goods can be sold only at a lower price, p. Because of the lowering of the prices, however, several plants whose costs of production are higher than the price level p cannot operate with profits; they have to shut down. The drop in production is represented by OC. The decrease in the available quantity of goods from OB to CB will cause an increase in the price up to P'. This again raises the production to NB, which in turn tends to press the price down, etc. The result is a fluctuation of production and prices around a center line, which we shall call a condition of equilibrium. Our figure enables us to decide whether the fluctuations diminish or even entirely cease. In that case a new status of equilibrium is obtained and therefore the disturbance dies down. If the oscillations increase, however, not only will no equilibrium be obtained, but the development leads so far that p falls below c', which means that because of too low prices all production ceases. The first case applies when OC becomes smaller than AB and when OP' becomes smaller than OP. The latter case applies when the drop in production is greater than the preceding increase of production and when therefore the price tends to pass over the original price level.

The following equations can be arrived at from this analysis:

$$\begin{aligned}
 \text{I:} \quad & \text{OA} : \text{OC} = (\text{OP} - \text{Ac}) : \text{Pp} \\
 & \text{OC} = \frac{\text{OA} \cdot \text{Pp}}{\text{OP} - \text{Ac}} \\
 \text{II:} \quad & \text{OB} : \text{OA} = (\text{OP} - \text{Bc}') : (\text{OP} - \text{Ac}) \\
 \text{or, } & (\text{OB} - \text{OA}) : \text{OA} = (\text{OP} - \text{Bc}' - \text{OP} + \text{Ac}) : (\text{OP} - \text{Ac}) \\
 & \text{OB} - \text{OA} = \text{AB} \\
 & \text{AB} = \frac{\text{OA} (\text{Ac} - \text{Bc}')}{(\text{OP} - \text{Ac})}
 \end{aligned}$$

Under the assumption that the line of costs is a straight line, OC is larger than AB if Pp exceeds Ac - Bc', or if the decrease in production (caused by the fall of the prices) is greater than the preceding increase in production, when the fall of prices exceeds the fall of production costs through technical improvements in the most efficient plant.

How far the prices fall depends on the elasticity of demand. We take the formula for the elasticity $xy^n = C$ from Marshall,¹ x meaning the quantity of goods produced, y the price, and n the elasticity.

By accepting elasticity as 1 we obtain the following result:

$$OA \cdot OP^1 = OB \cdot Op^1; \quad Op = \frac{OA \cdot OP}{OB}; \quad OP - Op = Pp = OP \left(1 - \frac{OA}{OB}\right)$$

According to equation II:

$$\frac{OA}{OB} = \frac{OP - Ac}{OP - Bc'}$$

Therefore:

$$Pp = OP \left(1 - \frac{OP - Ac}{OP - Bc'}\right) = OP \frac{Ac - Bc'}{OP - Bc'} = \frac{OP}{OP - Bc'} (Ac - Bc')$$

Since $OP > OP - Bc'$, $\frac{OP}{OP - Bc'} > 1$

Therefore Pp is greater than $Ac - Bc'$ and OC is greater than AB . The rise in price after the exclusion of the producers OC is easy to calculate:

$$CB \cdot OP' = OA \cdot OP$$

From $OC > AB$

it follows $CB < OA$

Therefore: $OP' > OP$

At the price P' not only are all plants OC working on a profit basis, but also those plants which could not produce at the initial stage and which we included in our figure by extending it as a broken line to the left beyond O . We take for granted here that equipment for production always exists, which equipment could be used without profits, as, for example, older machines, abandoned pits and the conversion of plants. To this belongs also, to a certain extent, the production of substitutes. If the prices rise, production can readily be increased through the use of this already existing equipment.

Because of this further increase in production, the price falls below p and the production under CB . The fluctuations have there-

¹ Marshall, Alfred, *Principles of Economics*, 8th ed. (London 1930) p. 840.

fore the tendency to swing away from the new equilibrium if the mechanism functions without friction. This tendency becomes stronger if, through the same increase in production, the price level is pressed still further down than we at first assumed.

On the contrary, the fluctuations tend to become smaller and to approach an equilibrium if the price level remains more stable. A new equilibrium will the more readily be established the greater the elasticity of the demand, as the following equations demonstrate.

Using elasticity n , we have:

$$\begin{aligned} OA \cdot OP^n &= OB \cdot Op^n \\ Op &= OP \sqrt[n]{\frac{OA}{OB}} \\ OP - Op &= Pp = OP \left(1 - \sqrt[n]{\frac{OA}{OB}} \right) \end{aligned}$$

Because $\frac{OA}{OB} < 1$, $\sqrt[n]{\frac{OA}{OB}}$ is larger, the greater n is. Therefore Pp is smaller, the larger n is and, according to equation I, OC becomes smaller, the larger n is.

With the same elasticity of demand the fluctuations in the quantity of production can be considerably influenced by the shape of the curve representing costs. It is clearly evident that the quantity of production is decreased less, the smaller the proportion of producing plants with high costs of production in relation to the total production. It is further obvious from *a* and *b* in Figure 2 that the equilibrium is the more difficult to obtain, the greater the number of single plants or groups of plants with the same costs of production. There is no basis for any equilibrium whatever in the case of a fall in price from P to p , as shown by *d* in Figure 2.

The tendency for production and price fluctuation to approach a stable equilibrium is independent of the reduction in costs in the most efficient plant. The condition of the marginal plants alone is the determining factor. The equilibrium is more stable when the marginal plants are smaller and is less stable when they are

larger. The latter situation exists, for example, in the competition between the automobile and the railroads.

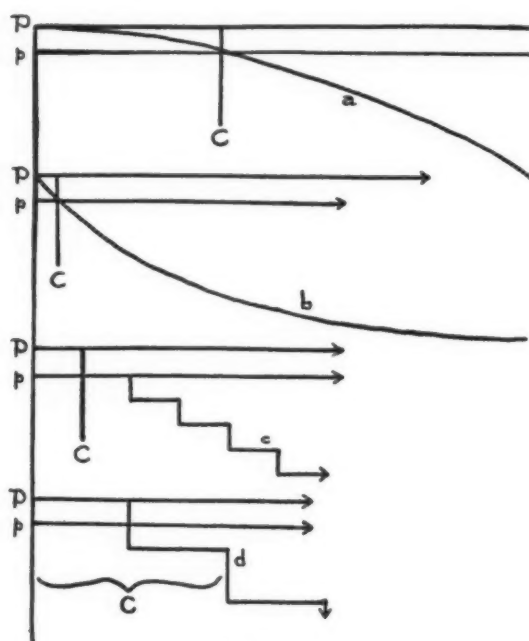


FIGURE 2

We can now do away with the assumption that costs of raw material and wages do not change.

Before the new plant begins to produce, it develops an additional demand for raw material and labor. Because of this the costs of production for all plants rise. In our scheme the line representing costs is shifted upward. At the price level P production in marginal plants is stopped. There follows a decrease in production, OD . According to the assumption that the prices of raw material and labor do not change, there results no decrease in production. The other extreme exists when all the laborers are occupied and the production of raw materials cannot be increased. In this case the new plant must increase wages and the prices of raw materials sufficiently to draw the workers and the raw materials

from the marginal plants. Since the proportion of costs in the price of a single product is larger in the case of a marginal plant than in that of the most efficient plant, or, since for the production of the same amount of goods in the most efficient plant less labor, etc., is used than in the marginal plant, the drop in production as a result of the rise in costs is in every case less than the increase in production as a result of the operation in the most efficient enterprise.

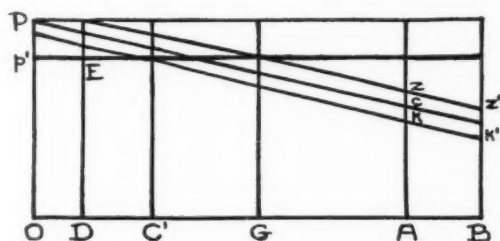


FIGURE 3

According to Figure 3, costs of production = $OP \cdot OD = Ac \cdot AB$

Since $OP > Ac$
 $AB > OD$

The total production DB is greater than the original production OA. The price of the product p' becomes therefore lower than the price before the opening of the new plant. As a result of the decrease in price the production falls again to GB. All these plants begin a new period of production with the purchase of raw materials and the engagement of laborers. Since not all the raw materials and laborers can be occupied until all plants DB are operating, when only the plants GB appear in the market for these means of production, their price, and therefore also the costs of production, must be lowered. The line representing costs in our graph must reach the point E. In this case a balance is struck. No plant produces at less than the costs of production and the last of the producing plants is identical with the marginal plant. Plants with higher costs of production therefore cannot open.

The more rigid the supply of means of production, especially labor, the more easily is the equilibrium established after a disturbance through an increase in production as a consequence of the introduction of new plants. The higher the wages rise through the opening of new plants, the less will be the fall in prices of the goods produced. The lower the costs of production fall below this level, the more rapidly will all elements of production be used again in their original function.¹ If the elasticity of the supply of elements in production is greater than zero, a fluctuation in production and prices will set in which, in the case of less elasticity, would tend toward an equilibrium,² but in the case of greater

¹ Here we pass over the whole group of problems which arise from the shift in income from wage earners to profit receivers; that is, we assume that the employers will use their increased income in the same manner as the workers.

² Where elasticity of the costs of production and the price of goods produced equals 1, an equilibrium is obtained after some fluctuations as can be seen from the following study:

$$\text{I: } OC' : OA = (Pp' - ck) : (OP - Ac)$$

$$\text{II: } AB : OA = (Az - Bz') : (OP - Ac)$$

If the elasticity of costs of production is 1:

$$\text{III: } OA \cdot Ac + (OP - Ac) \frac{OA}{2} = \frac{OA}{2} (OP + Ac) = \frac{DB}{2} (OP + Bz')$$

$$DB = \frac{OP + Ac}{OP + Bz'} \cdot OA$$

If the elasticity of prices is 1:

$$\text{IV: } OA \cdot OP = DB \cdot Op'$$

According to equation III:

$$\begin{aligned} OA \cdot OP &= \frac{OA(OP + Ac)}{OP + Bz'} \cdot Op' \\ \frac{OP + Ac}{OP + Bz'} &= \frac{OP}{Op'} \\ (OP + Ac) - (OP + Bz') : (OP + Ac) &= (OP - Op') : OP \\ (Ac - Bz')OP &= (OP + Ac)Pp' \\ Ac \cdot OP - Bz' \cdot OP &= Pp' \cdot OP + Ac \cdot Pp' \\ - Bz' &= \frac{Pp' \cdot OP + Ac \cdot Pp' - Ac \cdot OP}{OP} \\ &= Pp' - \frac{Ac \cdot Op'}{OP} \\ Az - Bz' &= Az + Pp' - \frac{Ac \cdot Op'}{OP} \end{aligned}$$

elasticity, on the contrary, has the tendency to increase so that no equilibrium in this branch of industry can be obtained. This leads again to our original proposition.

The changes in the quantity of money which result from changes in the volume of money can only be touched upon here. The quantity of money or its velocity of circulation changes when the purchase of raw materials and the payment for work takes place through the use of short term loans, if a rise in the demand for such loans is not satisfied through a rise in savings but rather by newly created bank credit. From the additional quantity of money only a portion is directed toward that branch of production whose expansion caused the increase in the quantity of money. How much of the new money flows back to this industry depends upon the elasticity of the demand for the goods produced in this industry. If the additional demand is only concentrated upon these goods, then the whole of the additional money will return, but if the elasticity is zero, then the additional quantity of money will raise the prices of elastic goods. When elasticity equals 1, this part of the additional quantity of money will return to the branch of industry of our example which corresponds to the share of its production value in the whole economic production value (i.e. in the national income). For example, if this share represents 10 per cent and if the rise in prices in this branch of production is also 10 per cent, then prices rise less than 1 per cent, since the costs make up only a part of the price of the goods. Because of these relatively small dimensions, therefore, this variable can be neglected in our scheme.

According to equations I and II:

$$OC' : AB = (Pp' - ck) : (Az - Bz') = [Pp' - (Ac - Ak)] : (Az - Bz')$$

Since $Az > Ak$ and $-\frac{Op'}{OP} Ac > -Ac$

$$(Az - Bz') > (Pp' + Ak - Ac)$$

$$\text{and } AB > OC'$$

or $C'B > OA$ (The fluctuations in the quantity of production tend to cease.)

Because of the new production $C'B$ the price will be raised from Op' to OP' .

$$\text{Since } C'B \cdot OP' = OA \cdot OP$$

$$OP' < OP$$

(The fluctuations of the prices tend to cease.)

Within these limits the fluctuations in the quantity of money operate in the following manner: a rise in the costs of raw material and wages in the whole industry (whether as a consequence of greater production or higher raw material and labor costs), and therefore an increase in the working capital, lowers the prices less sharply than it would with an unchanged quantity of money. According to Figure 3, Op' becomes therefore somewhat larger. Through it the drop in production, OC' , becomes smaller. As a result of the cessation of work in the plants OC' the amount of credit decreases. Since, nevertheless, the proportion of the costs of production in the price of the product is much greater in the plants OC' than in the technically more perfect plants AB , the decline in the demand for means of credit becomes greater than the prior increase. If, therefore, the fluctuations approach an equilibrium, this equilibrium will lie lower, that is, the volume of production will be depressed. If, through a decline in the rate of interest, a new expansion in production is not effected, it is entirely possible that a disturbance of the equilibrium through an increase in production will lead ultimately to a decline in real income.

We reach the same conclusion if we proceed on the theory that with a transference of production from technically imperfect to better equipped plants a transference from wages to profits takes place. Since in general wages have a greater velocity of circulation than profits and interest, the available quantity of money declines. Since through the fall in prices the wages also decline and therefore the credit again shrinks, there results a downward tendency in prices and production. These questions lead far into the theory of business cycles if they are extended from a single industry into the whole economy.

It seems consequent, from a consideration of this study as a whole, that it is by no means necessary that in each case a new equilibrium be established after the disruption of the economic balance. We perceive rather, that with a stable quantity of money an equilibrium in the production of commodities with inelastic

demand can hardly again be reestablished, while this possibility increases, the greater is the elasticity in the demand. An equilibrium can further be attained through a favorable grouping of plants according to their costs of production, namely, when the costs of production of the marginal plants show considerable differentiation. Besides, it certainly cannot be doubted that the fluctuation in production and prices can be brought within limits if remedial measures are taken, which in the nature of things is not possible in a system of free competition. The most extreme example is the limitation of production and the fixing of prices. Between the extreme cartel system and extreme free competition there are none the less a great number of intermediate stages, such as limitations upon the market, knowledge of competition, in the field, of the methods of production, of supply and even also of demand. This can lead perhaps to the fixing of prices on the part of the most efficient plant, by which a certain number of the marginal plants are excluded from production so that under the most favorable circumstances an equilibrium is immediately established. During periods of depression the fluctuations can be controlled so that production by unprofitable plants is maintained to some extent, perhaps even by subsidies, with the result that a rise in prices is prevented.

If increasing production is a function of technical progress, then perhaps it can be said that under free competition improvements in production and lower prices for commodities with an inelastic demand hinder and restrain rather than promote the development of the whole economy.

LITERATURE OF THE NEW DEAL

"Good publicity is a prime requirement for good statesmanship. A public man must get his story told." These words, quoted from an article by Paul Kellogg in the *New York Times*,¹ express a fundamental rule of the technique of modern policy. It ought to be understood primarily by democrats, whose task it is to enable the mass of the people to participate in the everyday problems and endeavors of the state. In our times, unfortunately, this task is often forgotten in democracies, while modern dictators, Bolsheviks and fascists know how to employ in a masterly way all the most refined methods of "propaganda and enlightenment." Indeed, it is by their methods of dominating and incessantly occupying the minds of men that the German fascists and Russian Bolsheviks justify their claim to being the most highly accomplished democracies in the world.

President Roosevelt knows well how immensely important it is to get his story told. Accordingly, in spite of the vast mass of his conventional duties he has undertaken to tell the story of the first year of his administration. His recent book² does not pretend to add to his earlier statements of policy and principle. It is not, as one might have hoped, a systematic exposition of the ideas that animate his policy. As the author states, "This book, without argument and without extended explanation, seeks to set forth simply the many significant events of a very busy year." It is a chronicle, consisting mainly of the original proclamations, messages, addresses and statements of the President. All these utterances, which had been scattered through the newspapers and were difficult of access, are here collected. One may profitably re-read them, from the proclamation closing the banks and the abandonment of gold through the whole alphabet of the New Deal. Yet one does not find answers to one's questions as to the real meaning of the various measures and their organic relations. Thus, when Mr. Roosevelt writes on the depreciation of the dollar, "that we proposed to maintain our currency and that at the same time we had determined definitely to seek an increase in all values . . . that the dollar was as good a dollar as it had been before, and that, in fact, we proposed to make it a more honest dollar," one may be pardoned for suspecting the presence of contradictions. None the less one is impressed again by the stupendous activity of the President, who bears with a smile the whole responsibility for all that has happened in a truly "busy year."

¹ *New York Times Magazine*, November 19, 1933.

² Roosevelt, Franklin D., *On Our Way*. New York: Day. 1934. 300 pp. \$2.50.

There has been no lack of other writers who have sought to present in intelligible terms the record of an amazing year in American economic policy. Looker¹ devotes himself particularly to the antecedents of Franklin Roosevelt: how he became President. Lindley² gives a more detailed description of the President in action. The two books are complementary in the glorification of their subject. Mr. William MacDonald³ tells the story of the year from the opposite point of view. For him, "the fruits of the program have been some artificial stimulation of business and industry, some artificial relief for the farmers, and some artificial mitigation of unemployment and personal suffering, but in their pursuit the Administration has become a dictatorship, the public debt has been swollen to unprecedented peacetime proportions, the gold standard has been abandoned, and the dollar has been left to find its level in the shifting sands of commodity prices. There is no dictionary that defines 'recovery' in such terms." He criticizes severely the different items making up the New Deal. Sometimes his reasons are convincing and the facts he adduces are significant. Unfortunately, in his zeal for establishing the defectiveness of one point of policy after another, he lays himself open to the charge of being one of the unreconstructed addicts of "laissez faire." Finally there is a slender volume by Beard and Smith.⁴ These authors recognize that action was imperatively required, because they clearly realize the sufferings of the people through the crisis. What they give is a comprehensive description of what has been done. Their work is objective, cautious in its conclusions and attentive to the future consequences of the President's policy.

It is not the main object of these popular works to examine the economic results of the New Deal. The international consequences are at best considered incidentally. On July 3, 1933, in a message to the World Economic Conference in London, the President declared that he would "regard the collapse of the Conference as a catastrophe amounting to a world tragedy." In fact, however, the isolation or, as Beard and Smith put it, the insulation of the national economies was only intensified later on, without much concern over the resultant tragedy. So far as concerns national policies Roosevelt disarms his economic critics by

¹ Looker, Earle, *The American Way. Franklin Roosevelt in Action*. [With an introduction by Colonel Edward M. House.] New York: Day. 1933. 382 pp. \$2.50.

² Lindley, Ernest K., *The Roosevelt Revolution. First Phase*. New York: Viking. 1933. 328 pp. \$2.50.

³ MacDonald, William, *The Menace of Recovery. What the New Deal Means*. New York: Macmillan. 1934. 401 pp. \$2.50.

⁴ Beard, Charles A., and Smith, George H. E., *The Future Comes. A Study of the New Deal*. New York: Macmillan. 1933. 178 pp. \$1.75.

repeating again and again that "the individual parts in his planned program are by no means inflexible or infallible. In some respects we may have to change the method; in others we may not have gone far enough. Time and experience will teach us many things." In similar vein he said in his message to Congress on March 16, 1933, requesting agricultural adjustment: "I tell you frankly that it is a new and untrodden path, but I tell you with equal frankness that an unprecedented condition calls for the trial of new means to rescue agriculture. If a fair administrative trial of it is made and it does not produce the hoped for results I shall be the first to acknowledge it and advise you." To be sure, the retreat from a position taken inadvisedly would not have remained wholly within the President's discretion. Every act of this character necessarily creates powerful interests that inevitably resist change. But it seems to be unanimously agreed that in the terrible plight of the country in March 1933 the question was not so much whether the means applied were the best discoverable. What was of decisive importance was that some means should be applied, that activity should be aroused, replacing the discouragement of the people and giving them a new hope and a new vision. If the development of the President's policy did not follow the precepts of the economists, it is pertinent to inquire, when has practical policy ever paused for the opinions of the economists? The present world crisis has been of such a character as to emphasize more emphatically than ever the wisdom of modesty on the part of the economists. In a crisis so disastrous the general suffering and despair may reach a point where it is preferable to give up even admittedly sound economic principles than to slip into a revolution which may destroy something of vastly more importance than any theory, however sound.

Most of the popular writers about the New Deal are, to be sure, not so much interested in the New Deal as a set of economic measures as they are in the structural changes which in the long run may come out of it. The man in the street usually—though erroneously—identifies the New Deal with the NRA. Often he disregards the ultimate significance of the agricultural and the monetary policies of the New Deal which may affect the structure of society quite as powerfully as the NRA. But the NRA, in content and method, is strongly reminiscent of the economic organization for war, and it appeals to similar popular emotions. Like the war organization it admits state interference in a measure unprecedented in peace time; it appeals for social cooperation and discipline. Moreover, the NRA, more than any other of the New Deal policies, is directly concerned with what is conceived to be essential

in capitalism, the relation of industry to the state, the position of labor in capitalistic industry.

This concentration upon the NRA characterizes also the scientific writing on the New Deal. In its publication, *The ABC of the NRA*,¹ the Brookings Institution presents a very instructive survey of the act itself and of its administration, with the most important documents added as appendices. Mayers' *Handbook of NRA*² is a compendium of detailed information answering both practical and scientific requirements. A literature is also developing which deals with the most urgent problems of the NRA. Whitney writes on *Trade Associations and Industrial Control*³ and traces the steps leading from the trusts and the trade associations to the codes of fair competition. Terborgh examines the problem of *Price Control Devices in NRA Codes*.⁴ Daugherty⁵ gives an account of the history and content of labor regulations under the NRA; Stein, Raushenbush and MacDonald⁶ offer a study of the legal precedents for the NRA labor policy and endeavor to forecast the future attitude of the courts.

The popular studies cited above are extremely positive in their criticism or defense of the New Deal. Thus MacDonald, whose position is hostile, writes: "With the exception of the five-year plans of Soviet Russia and the corporative plan of economic organization for Italy, no statute or decree of any modern state has gone so far as this one in subjecting industry and trade to government control, or made union labor so important a factor in wage contracts and working conditions, or imposed so drastic a restriction upon the conduct of business of any kind for profit."⁷ The supporters of the New Deal are equally im-

¹ Dearing, Charles; Homan, Paul T.; Lorwin, Lewis L.; and Lyon, Leverett S. *The ABC of the NRA*. Washington: Brookings Institution. 1934. 185 pp. \$1.50.

² Mayers, Lewis, ed., *A Handbook of NRA*. 2nd ed. New York and Washington: Federal Codes. 1934. 841 pp. \$6.50; with semi-monthly supplement service, \$10. (An analysis and compilation of the National Industrial Recovery Act and related statutes, federal and state, and of all executive orders, regulations, agreements, administrative rulings and judicial decisions relative thereto; together with a comparative presentation of typical provisions of the several codes of fair competition, the texts of the principal codes and summaries of all minor codes.)

³ Whitney, Simon N., *Trade Associations and Industrial Control. A Critique of the N.R.A.* New York: Central Book Company. 1934. 237 pp. \$3.

⁴ Terborgh, George, *Price Control Devices in NRA Codes*. Washington: Brookings Institution. 1934. 45 pp. 50 cents.

⁵ Daugherty, Carroll R., *Labor under the NRA*. Boston: Houghton Mifflin. 1934. 38 pp. 25 cents.

⁶ Stein, Emanuel; Raushenbush, Carl; and MacDonald, Lois. *Labor and the New Deal*. New York: Crofts. 1934. 95 pp. 75 cents.

⁷ MacDonald, William, *op. cit.*, p. 164.

pressed by its far reaching effects. But the scientific studies show clearly that the whole policy is in a state of flux. Terborgh's survey indicates that the organization of American industry under the codes is now moving rapidly in the direction of the German cartels. In an astonishing number of codes the cartel methods of price control, of control and limitation of production are applied. But there is one decisive difference. The German cartels with very few exceptions arose as voluntary organizations and therefore the possibility of actual or future competition by outsiders remained. The organization of all American industry under the codes comprehends without exception every plant in the industry and, through moral and social pressure, participation in the organization is compulsory. The law protects those engaged in several industries against members who might wish to expand their business as well as against outsiders seeking to enter the field. It is the intention to protect alike the weak and the strong, the efficient and the inefficient. But the method already often involves the assignment of production quotas; and from this it may not be a long step to the practice usual in German cartels, whereby the strong concerns buy up the quotas of the weaker ones. In many cases the German cartels exhibited a powerful tendency toward concentration, horizontal and vertical, with the result of emphasizing the predominance of the big enterprises at the expense of the smaller ones. Under the NIRA, to be sure, governmental control has freer scope, in theory, than under the German cartel system. But the question, what forces lie behind government control, rises to vex us. Through their social and political power, the organized industries themselves may in effect determine the operation of control. The histories of the oil code, the iron code, the automobile code are instructive in this connection. The position of organized labor under the codes raises the same question. Whatever the intent of the law, the fact remains that in a great many important industries the regular unions are not recognized and that the problem of the company union is still unsolved. It is further worth bearing in mind that of the hundreds of code authorities only an insignificant number contain employee representatives and only two authorities contain representatives elected by independent trade unions.¹ As Daugherty concludes: "The partnership thus far is, in the great majority of industries, between the government and industry, and labor will cease being an outsider only when it becomes strongly organized and possesses real economic power."² He recognizes, however, that the failure of organized labor to function in

¹ Stein, Raushenbush and MacDonald, *op. cit.*, p. 11.

² Daugherty, *op. cit.*, p. 20.

connection with the codes is due not only to the effective organization of the employers, but also to the internal weakness of the existing labor organizations. To quote again: "The vital questions still remain to be answered: Are American unions properly equipped in structure, function, and leadership to consolidate their gains and go still farther? Has the NRA done and will the NRA do anything about the antiquated craft form, the old fashioned anti-social and futile tactics, and the generally weak and sometimes dishonest leadership?"¹

Through all the literature on the New Deal, but particularly in the popular literature, questions of a more general nature are constantly emerging. Is the New Deal the beginning of a system of planned economy? Does it represent a revolution, if not silent, at least, down to the present, bloodless? Is a putative rugged individualism giving way to bureaucracy and regimentation? Is the animus of the New Dealers communistic or fascist: or if they are unaware of their animus, do their acts accumulate toward communism or fascism? Like the man in the street, most of the writers of the popular books on the New Deal give or suggest answers to these questions with a degree of assurance hardly warranted by the available facts. But Beard and Smith wisely say, "At best the (recovery) program can only be regarded as the beginning of a transition."² The beginning of a transition—to what? For the time the question remains open.

ARTHUR FEILER

¹ *Ibid.*, p. 36.

² Beard and Smith, *op. cit.*, p. 170.

BOOK REVIEWS AND NOTES

HOMANS, GEORGE C.; and CURTIS, CHARLES P., Jr. *An Introduction to Pareto. His Sociology*. New York: Knopf. 1934. 300 pp. \$2.50.

It is very difficult to read Pareto's *Trattato di Sociologia Generale*, which will soon be presented to the American public in an English translation. This huge work lacks order, its nomenclature is intentionally odd, and the interrelations of the concepts are neither completely worked out nor consistent. An introduction to the book, the importance of which will for political reasons be variously estimated, can be valuable only if all simplification of Pareto's ideas is avoided. For Pareto popularized is but an ideologist of fascist politics; his scientific attitude which actually has nothing to do with fascism then becomes obscured.

Homans and Curtis modestly state that nearly everything in their book that is not Pareto's they owe to Professor Lawrence J. Henderson at Harvard, who has conducted a seminar on Pareto for the past two years. Their own achievement consists in a systematic arrangement of Pareto's main ideas and of the discharge of the mathematical ballast with which the Italian scholar presented them. This has been done successfully. It is natural and excusable for scholars who have worked over so vast and difficult a body of material as Pareto's work to place a higher value on their subject—and on their own acumen in perceiving this value—than the mere reader can accept. When reading this book one cannot fail to receive the impression that the authors find great satisfaction in being let into the secrets by means of which society and history are made to appear a kind of Frankenstein, a living mechanism which could not be controlled until Pareto's treatise appeared. "Pareto may be," they say, "the Copernicus of society." They admit that they are amateurs, but they do not hesitate to criticize sociological science for not having yet reached the stage of "mathematical puberty." Neither do they take cognizance of the fact that very many sociologists regard the treatment of social phenomena by methods borrowed from the natural sciences as a fundamental failure, no longer interesting at all except for the historic circumstances in which this error arose.

The authors do not even recognize what are after all the most important tasks in a study of Pareto, the determination of the place of his methodology in the history of sociology, and the critical analysis of the results attained with it. They develop, for purposes of refutation, a possible critique on Pareto's theory of the residues, for instance, but this critique is so weak that it is easy for them to refute it. One of the

chief problems, the relation of sociology to history in Pareto's system, is not mentioned at all despite the fact that the authors meet it again and again. Once they comment that "the choice of a particular derivation to gain a residue-in-chief with the conclusion required to confirm it depends on the emotional and intellectual atmosphere" (p. 176). What is this atmosphere if not a convenient escape from the necessity of facing the shortcomings of Pareto's non-historical approach to social facts?

The authors have largely substituted instances taken from modern times for Pareto's own vast and varied mass of historical examples, the analyses of which form the most interesting parts of Pareto's sociology. They wish to show that Pareto's theory is applicable to our social and political life, but their examples weary the reader because only a few are cleverly chosen.

Homans and Curtis say nothing new even to those who have read only Bousquet's introductions to Pareto in English or German. Their book is not of great scientific value. It might lure laymen into adding some fashionable terms of psychology to their vocabulary, but it is to be hoped that Pareto's concepts, "persistent aggregates," "residues of combination," "non-logico-experimental action," will not appeal so much to the public as did the Oedipus and inferiority complexes of psychoanalysis.

HANS SPEIER

OGG, FREDERIC A. *European Governments and Politics*. New York: Macmillan. 1934. 905 pp. \$4.25.

The great number of thorough works in the English language which present comparatively the constitutions and governments of the major European countries is surprising to the European student of political science. The literature of continental Europe, which should be more interested in such studies than America, does not contain an equivalent body of works. One of the foremost American writers in this field, Professor Ogg, has now crowned his former works on *The Governments of Europe* (New York 1913, 2nd ed. 1920) and *English Government and Politics* (New York 1929), with a comprehensive treatment of *European Governments and Politics*. This work is not designed to replace its precursors but follows an independent plan. It embraces five countries, Great Britain, France, Germany, Italy and Russia, and presents facts and figures down to 1934. The book represents a thorough examination of working forces, of their institutional and historical basis, and of the problems involved, with comparative discussion.

Ogg does not follow the plan adopted by Finer in his *Theory and Practice of Government* (London 1932) of organizing his material in chapters dealing with institutions as they appear in the several countries studied. Instead, he treats the several governmental systems as organic entities. Great Britain naturally occupies the largest space, with 434 pages, or nearly one half of the whole volume, France and Germany are given 206 and 167 pages respectively, Italy and Russia are restricted to about 40 pages each. The chapters on Great Britain cover essentially the ground of Ogg's former work but bring it down to date and compress the material to make place for valuable additions. The additional material contains a detailed explanation of the British constitution and government.

The French part, though more compact, has the same merits. There are indeed some points in constitutional history, for instance the episode of President MacMahon and the forced resignation of Millerand, that might well have received more attention, since acquaintance with them is indispensable to an understanding of the working constitution.

The section on Germany is really a great achievement. Ogg states, in a preface, that this part offered the greatest difficulties. His former work in its first edition had to deal only with the monarchy; in its second edition, with the Weimar democratic republic besides. In this work the National Socialist state also had to be analyzed. The author modestly represents the section on Germany as a mere "moving picture of a great people feeling its way hazardingly along the high road of political experience." He succeeds admirably, however, in drawing a rather complete picture of all three constitutional systems. There is no work in Germany which covers the whole field so adequately in a similarly limited space. This work is done competently, but a German will not agree with all the author's evaluations. Bismarck, for instance, is viewed casually in a typically un-German way, as a man who in 1864 knew exactly what would happen in 1866 and 1870 and proceeded cynically to realize that sequence of events. But in general the author endeavors to keep strictly to the merits of the case and has avoided easy generalizations and preconceived opinions. The author and his two co-workers on the German part, Professor L. Kirk and Miss Katharine Reimann, deserve high praise for the fairness of spirit in which they have carried through this part of the work.

The shorter chapters on Italy and Russia will serve as a good introduction to the study of the historic and political development, the actual working of these governments and their chief trends. Especially the chapters on Italy are brilliantly executed.

In so extensive a work there will naturally be numerous minor details to which a meticulous reader may take exception. Legislation by royal proclamation during the Tudor and Stuart periods might have been discussed more thoroughly, as not only historically but theoretically interesting. That the British civil service after the reforms in the second half of the nineteenth century was "the first truly expert and professional civil service known to the Western world" (p. 150) may be disputed; the Prussian civil service, justly praised in another place (p. 662) for its orderliness and efficiency, deserves that credit. The excellent British civil service is further somewhat too highly praised as being recruited from no special classes (p. 164). Although the conditions have been much liberalized it is still the Oxford and Cambridge type of man who is favored. It would have been worth while to give the reasons why the electoral reform bill failed in 1930: the conflict between the Labor government and the House of Lords (p. 204). The House of Lords is said never to have used devices for bringing debate to a close (p. 258); but such devices have been applied on occasion during the last decade. Private bills in the technical sense have never played a part in the German Reichstag—contrary to what is said on p. 270—because of the extensive home rule rights of the communes and the eventual powers granted to the supervising authorities. Among the reasons in favor of administrative tribunals (p. 370) it might be added that these courts are composed of experts knowing the administrative work from their own experience.

I should not agree with the suggestion in favor of proportional representation for France (p. 539; cf. my article, "Constitutions and Leadership," in the August number of *Social Research*, p. 279). The statement that the German Empire had no cabinet might have made allowance for the so-called war cabinet introduced by Prince Max von Baden (p. 657). For February 1919 the term chancellor is an anachronism; at that time there was only a prime minister (p. 675). That Bavaria and other southern states were "separatist-minded" by 1919 is saying too much (p. 689). Ogg emphasizes the fact that the national government could independently withdraw any and all powers from the states, including their territories (p. 692). But this could only have been done by altering the constitution. The abolition of the diets of the Länder was not proposed by the conference for Reichsreform of 1928, except eventually for Prussia and the smallest units. Presidential ordinances based on Article 48 were not proclaimed from 1925 to July 1930, with the exception of repeals of former ordinances (p. 712). The last Prussian quota in the Reichsrat was 26 votes, not 27 (p. 747). All govern-

mental votes could be cast only in an indivisible block (p. 747). The National Socialist party did not capture 32 seats in the Reichstag of 1924 as against 12 in 1928, as the author claims (p. 774); the figure for 1924 includes other racial parties.

These minor details are, however, of no weight against the solid merit of Ogg's book. It is a masterpiece of acumen, accuracy and extraordinary command of the literature.

ARNOLD BRECHT

LLEWELLYN, KARL N. *Präjudizienrecht und Rechtsprechung in Amerika*. 2 parts. Leipzig: Weicher. 1933. Part I (text), 122 pp.; Part II (cases and materials), 350 pp. Paper, 18 RM; cloth, 21 RM.

This book begins with a thorough description of the traditional American practice of deriving rules from precedents. It sets forth the delicate techniques of formalistic logic, by means of which any precedent may or may not be held applicable to the case. It explains to the foreign reader the characteristic features of the American court system and procedure. Upon this background the author develops his theory of legal realism: the traditional mechanical jurisprudence and its doctrine, that rules decide cases, cannot be maintained. It is impossible to predict by logic whether the courts will apply a certain rule to the case, or exclude it. The realist, therefore, by observing the past behavior of the judge, tries to find new methods to predict his future action.

The new practical science is the main subject of the book. Llewellyn gives a wealth of sociological observations, outstanding on account of their insight and their capacity of rendering in words the complexity of social events. Of special importance for realistic doctrine are the reflections upon legal certainty in case law. Here Llewellyn states, as decisively as anywhere else in his publications,¹ that there is no law separate from the substance of a case. What has been called a rule refers only to those decisions which previously have been rendered in its name. The rule is a "word symbol" (p. 76); its contents are elastic within certain limits that are set by the traditional ways of legal thinking. Every new application of this word symbol to another case changes the rule (p. 75).

This is the crucial point in Llewellyn's theory; here he has been criticized from different angles. Fuller² opposes his behavioristic

¹ Cf. Kantorowicz, Hermann, "Some Rationalism about Realism" in *Yale Law Journal*, vol. xliii (1934), p. 1240 ff.

² Fuller, L. L., "American Legal Realism" in *University of Pennsylvania Law Review*, vol. lxxxii (1933-34), p. 429 ff.

opinions on the nature of legal concepts. Kantorowicz¹ points out that the rule is a value judgment, which stands above the single case. Ascoli² stresses the political dangers of such decisionalism, especially in the field of constitutional law.

It is doubtful whether these and other critics who follow similar lines³ really are doing justice to Llewellyn. Two of his principal thoughts are obviously irreconcilable with his professed decisionalism.

1. Realism is designed to demonstrate to the judge how he may extend or restrict the contents of a rule. Llewellyn demands that this opportunity should be used and that the future development of the rules should consciously be directed in certain ways.⁴ The *Richtergewissen*, the conscience of the judge (*Präjudizienrecht und Rechtssprechung in Amerika*, p. 79), should be decisive. The judge, in applying the provisions of the constitution, should "control the course of governmental practice by reference to an ideal found . . . in the nature of what our government should be."⁵ The extensive interpretation of the due process clause "has been an enforcement of the majority's ideal of government-as-it-should-be."⁶

2. Llewellyn repeats on almost every page that the law should not lag behind the change in social conditions. His dislike for fixed rules is based upon the ever recurring assumption that life is in a perpetual flux. The same idea, seen from another side, is stressed in his observations on the layman's legal conscience. The layman, although he does not know anything about precedents, rules or traditional legal thinking, nevertheless will normally be able to foresee how a court would decide on his behavior. The reason for this, according to Llewellyn, is not that he knows the law but that he is aware of the *gesellschaftliche Normen*, the social norms (*Präjudizienrecht*, p. 82), that fix values at every step in life. These social norms are the basis of the judicial decisions. If the courts disregarded their development and remained behind the social trends continually, the layman would speak of a crisis in the legal administration (p. 83). This connection between law and mores might be highly objectionable (if Llewellyn means that law should be patterned only after the mores), but it shows quite

¹ Kantorowicz, *loc. cit.*

² Ascoli, Max, "Realism versus the Constitution" in *Social Research*, vol. i (May 1934) p. 169 ff.

³ Cf. Kantorowicz, *loc. cit.*, footnote 8.

⁴ Llewellyn, Karl N., "The Constitution as an Institution" in *Columbia Law Review*, vol. xxxiv (January 1934) p. 1 ff.

⁵ *Ibid.* p. 40.

⁶ *Ibid.* p. 39.

clearly that Llewellyn is not in any way a pure decisionalist. He knows that there are value judgments which bind the courts.

A reconsideration of the "word symbols" and "traditional legal thinking" now reveals that they imply more than Llewellyn's critics assume. Legal thinking comprehends, besides technical routine and customary approach, the process of discovering social norms, observing their development, and perceiving the ideals toward which the law ought to be developed. The "word symbols" are not merely a neutral formula; they are *Richtlinien* that indicate "the basis of experience and the accepted tendency of the further development of the rule" (p. 39).

The judge whom the realist likes must have training, conscience, responsibility, "an everlasting suspicion against his own prejudices," "an insight in the slight but most important advances that harmonize law and life" (p. 94). This is not the language of a man who disregards normative rules. Such words evince as clearly as possible that Llewellyn's realism is descended from the same pragmatic spirit, and from the same humanitarian ideals, as the sociological jurisprudence of men like Holmes, Pound or Cardozo. Like them he desires to achieve by trial and error, with the help of the social sciences, a legal development that follows the trends of social life and submits to the demands of conscience. Llewellyn's peculiarity is based upon only one point: he fights with all his resources against any mechanical reemployment of secured results. He does not recognize fixed rules, but accepted tendencies only.

Obviously Llewellyn overemphasizes the flux and change in law. There are many sections of life in which the same rules have been useful for centuries and may continue to be useful far into the future. It also cannot be denied that some of his formulations lead logically to conclusions which cannot be accepted.¹ However important these objections may be, they do not impair the value of his doctrine. He teaches us the never resting skepticism of the scientist. Our age, which is quick to observe the first indications of new developments, must be vigilant and must not trust in stored experience. The realists have been blamed from different sides for being the theorists for the attorney alone. As far as Llewellyn is concerned, this indictment is unjust. He tries to educate the judge to the needs of our time. His ideas and his sociological observations are of the highest pedagogical value and are a necessary counterbalance to the dogmatic nature of all teaching.

RUDOLF LITTAUER

¹ Cf. Kantorowicz, *loc. cit.*

HAIG, ROBERT MURRAY, and SHOUP, CARL. *The Sales Tax in the American States*. New York: Columbia University Press. 1934. 833 pp. \$4.50.

The most striking feature of the recent history of taxation is the fact that the sales tax has been introduced as an important link in the tax system of many nations. All belligerent European countries, with only one exception, adopted the sales tax between 1916 and 1923, in the fiscal emergency of the war and postwar years. Most of the American states introduced it in the emergency of the current depression. Probably every country is now considering increasing or remodeling the sales tax. It is therefore fortunate that the most recent experiences with the sales tax in the different states of the United States should be compiled and analyzed as they are in this work, which has been prepared, under the direction of Robert Murray Haig, by Carl Shoup with the assistance of other scholars. Only through well organized cooperation was it possible to draw conclusions from the experience of the last three years, at a time when it may be used as a basis for the actual tax reforms now considered in many countries. It is a pity that a corresponding comparative work of the same level has not been written on the much older European experience.

With the aid of a carefully developed terminology and classification, the provisions of the sales tax laws and sales tax administration are compiled and compared. The psychological and economic reactions of the taxpayer are explored with a questionnaire sent to many representative firms. The work offers not only a contribution to the economics of the sales tax, but also to its sociology and psychology. It is surprising how small is the resistance of the taxpayers to this tax as an emergency measure, particularly in comparison with their feelings as to an eventual increase of the income tax. According to the statements of the taxpayers, a great part of the sales tax cannot be shifted by the retailers, particularly by the smaller ones. To the writer this result is surprising. He believes that this condition can be due only to temporary friction. According to his theoretical expectation the sales tax, as a consumption tax, is bound to be shifted sooner or later. He even doubts that the statements of the taxpayers are a wholly reliable authority as to the facts of tax shifting.¹

This clash between theoretical expectation and empirical observation is perhaps one of the most interesting features of the volume. The

¹ It may be asked whether it would not be a useful supplement to the subjective method employed in this work to compare the price development of certain products in neighboring states with and without a sales tax.

reason for this rift between theory and experience may be that the sales tax has been treated in terms of the traditional theory of taxation. We cannot discuss here the theory of the sales tax. We may only raise the question whether this tax fits into the usual tax classification and the accepted theory of tax shifting, or whether it necessitates their revision. The theory of tax shifting has been developed chiefly in the field of excise and income taxes. If we regard the sales tax as representative of a third group of taxes, business taxes, we find that no general judgment as to its shifting is possible without consideration of the disposition of tax receipts on the one hand, and of the special market situation on the other. Such considerations lead us to assume that the tax may be shifted in some cases and not in others. Perhaps it is also necessary to revise the classical evaluation of the sales tax. Since Adam Smith charged the "Alcavala," the Spanish sales tax, with having caused the agricultural and industrial decline of Spain, authorities on public finance have argued against the sales tax without regard to the special fiscal and economic situation in question. There is no doubt that the sales tax will be used not only in times of emergency but will become a permanent part of the modern tax system. But the imperative task is to develop this crude tax into a flexible and pliant instrument of business taxation, as the old income taxes of the emergency times of the eighteenth century were refined step by step into the modern forms of income taxation. For this task the present volume offers valuable material.

GERHARD COLM

QUITTNER-BERTOLASI, ELLEN. *Das Verhältnis von Trend und Konjunkturzyklen als mathematisch-ökonomisches Problem*. [Veröffentlichungen der Frankfurter Gesellschaft für Konjunkturforschung, ed. by Eugen Altschul, new series, no. 7] Leipsic: Hans Buske. 1933. 57 pp. 3.65 RM.

This book which emanated from the seminar of Dr. Altschul discusses the interrelationship between the economic theory of the business cycle and the technical methods of trend calculation. In the first portion of the work, the writer presents a short review of the different methods of trend calculation and trend elimination. In the second portion, she analyzes the theories of development as promulgated by the economists, Ricardo, Say, Veblen, Schumpeter, Marx and Lederer. She concludes that the methods of trend calculation ordinarily applied do not correspond to the line of economic development which might be derived from these economic theories. Without outwardly favoring

any one of these theories, she states that the decline of business is a step in the process of adjustment on the road to a new upswing. She believes that economic development is a kind of interrupted growth which corresponds to biological growth, and is best described with the aid of the exponential linked curve. I cannot admit that she succeeds in proving that the shape of economic growth must really always correspond to that of biological growth. But even if there remains a doubt as to whether or not her solution is generally applicable, this cannot detract from the high value of her critical discussion. It cannot be sufficiently stressed that every statistical method must be based on the theoretical analysis of economic facts. The neglect of this point is very dangerous in the case of economic statistics, which borrows most of its methods from other sciences.

GERHARD COLM

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Eduard Heimann, *Arthur Feiler* and the reviewers, *Hans Speier*, *Arnold Brecht*, *Rudolf Littauer* and *Gerhard Colm*, are members of the Graduate Faculty of Political and Social Science.

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SOCIAL RESEARCH

*A Quarterly Journal published by the
Graduate Faculty of Political and Social Science
of the New School for Social Research*

ALL students of the social sciences are aware of the remarkable part played by the continental quarterlies, particularly the German, in the development of thought. In these organs have been published in brief form an extraordinary proportion of the ideas that have later been worked out in the bulky volumes that represent the final conclusions of their authors. Sometimes the magazine article has represented merely a chip from a scholar's workshop, a by-product of his activity, destined perhaps to become the center of the activity of a younger scholar. At other times the article has been the spearhead of the author's thought, a challenge to the learned world to note a new turn in ideas.

This creative role of the continental magazine existed only by virtue of the prevalence of academic freedom. This freedom has been publicly repudiated by three of the most important nations of Europe; its position is precarious almost everywhere east of the Rhine. The scholars who functioned creatively under the regime of liberty have been silenced or displaced. Hundreds of them are residing abroad, where they are valiantly rebuilding their shattered systems of life.

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